FINANCIAL HISTORY

The magazine of the Museum of American Finance

How Canadian Banks Avoided the Recent Financial Crisis

Beggar Thy Neighbor: A History of Usury and Debt

Wall Street on the Prairie

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IN THIS ISSUE FEATURES

IN THIS ISSUE DEPARTMENTS

ON THE COVER

Examining the difference between Canadian and US banks during the recent financial crisis. See article, page 13.

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2013 Begins With Record-Breaking Gala

Message to Members

David J. Cowen | President and CEO

2013 has commenced on several high notes. By all measures, our annual gala in January was the most successful to date. A record number of guests attended the event, and it generated more than $760,000, which smashed the previous record by over $200,000. We thank our honoree, Bill Harrison, and all of our trustees for their monumental efforts to achieve this ambitious fundraising goal. We would like to single out the support of the Geduld Cougar Foundation, which was unfortunately not recognized in the gala program. The funds generated by the gala are vital to the Museum, as they support all of its programs and operations, from events and exhibitions to publications and educational initiatives. Also, for the first time since its inception in 2008, the gala was featured in the Sunday Style section of *The New York Times*, thanks largely to the efforts of our pro bono public relations firm, Cognito.

I am also pleased to report the addition of three new board members, who were elected in February. Glenn Kaufman, president of Kaufman Family LLC, joins us as we continue the connection to his storied financial family; Brad Kopp has a passion for finance and history and is a career banker, most recently as the president of Butterfield Bank; and Richard Payne is vice chairman of Wholesale Banking at US Bancorp.

I would also like to thank two retiring board members, Charlotte Beyer and Steve Cooper, for their years of service. Charlotte and I joined the Museum at the same time, and her enthusiasm for the Museum's mission and the importance of financial literacy was evident from the start. She was the driving force behind the Museum's 25th anniversary thought leadership event at the NYSE in the fall and was an active participant in the development of the Museum Finance Academy. Steve served as a trustee from the Museum's earliest days and participated in the Museum's growth from its small gallery on Lower Broadway to its current 30,000 square foot home on Wall Street. We wish him the best, as he has established permanent residence in Florida.

In April the nation celebrates Financial Literacy Month, as we turn a spotlight on the importance of finance in our everyday lives. Sadly, the reality is that much of the American population is financially illiterate. The firm of Southport Lane is trying to do something about that, and they have agreed to underwrite free admission to the Museum on Saturdays for the remainder of the year. One of our goals has always been free admission, as we want everyone to have the opportunity to experience and understand the power and value of finance to the American economy and to their own lives. As good economists, we know that our visitor numbers usually double when we open the Museum for free. Free Saturday admission is a wonderful way to make the Museum and its programs accessible to all.

Lastly, we have come full circle with our "Alexander Hamilton: First Secretary of the Treasury" exhibition. The Museum first debuted this biographical exhibition on the founder of the American financial system in the US Custom House in 1989. The traveling version of the show, which includes reproduced paintings, engravings, correspondence and financial documents to reflect Hamilton's life and financial legacy, will be on display at the Union League Club in New York from April 11 through May 18. It will then be available to travel elsewhere, as we spread the message of the importance of Alexander Hamilton to the nation. This exhibition, like all of our others, is a central component of the Museum's core mission to preserve, exhibit and teach about American finance and financial history. $

Photo: Elsa Ruiz

David Cowen speaks at the 2013 gala.

APR 15 1954 Under a new law provision of the US Internal Revenue Code, April 15 becomes the due date for individual tax returns.

APR 10 1792 In the wake of the nation's first stock market crash, the New York State legislature enacts a law banning public stock auctions. The new law notwithstanding, stock trading continues.

Volunteer Spotlight: John Cirincion

By Kristin Aguilera, Deputy Director

Like most non-profits, the Museum relies on a corps of volunteers to assist in most aspects of its daily operations, from staffing the front desk and gift shop to giving tours and assisting with the archival collections.

Among the most dedicated of these is John Cirincion, who came to the Museum shortly after it opened at 48 Wall Street in 2008. John's background as an attorney working in several top financial services firms, including Merrill Lynch, AXA and an insurance subsidiary of Citigroup, made him a natural fit for the Museum. After completing the Museum's docent training program, he began giving guided tours of the permanent and temporary exhibitions to students, as well as professional and adult groups.

Kristin Aguilera

John's favorite aspect of his volunteer work at the Museum is interacting with the visitors and watching their faces light up as they learn new things and get to see unique historical artifacts. He counts among his favorite objects the rare piece of ticker tape from the 1929 crash, the 18-karat gold Monopoly set, the $100,000 bill and the five cent note with the portrait of Spencer Clark, who was the only living person ever to be depicted on US currency.

With the launch of the Center for Financial Education in 2010, John expanded his role at the Museum to include teaching classes. He can often be found teaching the "Financial Markets" course, a primer on investments, to high school and college students. In 2013 he began teaching one of the Museum's latest offerings, "The Role of the Capital Markets," to college students and adult groups.

In addition to his volunteer work at the Museum, John serves as a volunteer trustee at the New York Center for Autism Charter School in Manhattan and is a tour guide for Wall Street Walks. He is an enthusiastic Yankees fan, an avid traveler (Italy is his favorite destination) and a season ticket holder to the Metropolitan Opera.

Next time you visit the Museum on a Wednesday, be sure to say hello to John, and to thank him for his years of dedicated volunteer service. $

Museum Introduces Mobile Resource Center

By Elizabeth Blasi

The Museum has taken innovative steps to encourage the public to engage with selected financial artifacts in the exhibit hall and to address any emerging inquiries regarding exhibited materials. The Museum's new mobile resource center, called "The Exchange," is staffed by trained educators, docents and volunteers and promotes a better understanding of objects and documents from the Museum's collection.

Visitors are now able to tangibly investigate various materials and ask trained docents and educators any questions they may have during their visit to the Museum. Stocks and bonds were the central focus during the commencement of the new resource, where visitors were able to touch and examine qualities such as the diverse detailed engravings of the documents. As the assorted collection of stocks and bonds were passed around the first group to interact with the mobile resource center in March, identifying characteristics, such as the transfer obligation and the rights of the shareholder, were distinguished.

The Museum gratefully acknowledges ING for its support of this exciting new initiative, which will further enhance the Museum's capacity to interact with the visiting public. $

Elizabeth Blasi is the Museum's Ruth Baker Financial Education Intern.

Kristin Aguilera

Senior Educator Chris Meyers interacts with visitors at "The Exchange."

APR 2 1799 The Manhattan Company, a corporation founded by Alexander Hamilton and Aaron Burr that plans to supply New York City with fresh water, is chartered. It soon becomes the Bank of the Manhattan Company, ancestor of Chase Manhattan Corp. and later JPMorgan Chase.

APR 15 1998 The NYSE institutes its "circuit breaker" rules, mandating trading halts when the DJIA drops at least 10%.

Museum Honors Bill Harrison with Whitehead Award at 2013 Gala

The Museum honored William B. Harrison, Jr. at its annual gala in January with the 2013 Whitehead Award for Distinguished Public Service and Financial Leadership. The award is presented annually to a person who has demonstrated a high order of achievement and leadership in the field of finance, and also served with notable distinction in the public sector. It is named after John C. Whitehead, former Deputy Secretary of State and Co-Chair of Goldman Sachs who has headed numerous public service organizations.

"Bill truly embodies the spirit of the Whitehead Award," said Museum President David Cowen. "In addition to his important contributions as a financial leader, he has dedicated much of his time to meaningful charitable work."

The Museum's 2013 gala was the largest since its inception in 2008, with more than 250 people attending. In addition to Mr. Harrison, featured speakers included Erskine Bowles and Duncan Niederauer.

Mr. Harrison is the former Chairman and CEO of JPMorgan Chase, where he retired as Chairman at year-end 2006. Previously he had held the position of CEO of Chase Manhattan Corporation from June 1, 1999 and presided over the mergers with J.P. Morgan in 2000 and Bank One in 2004. He serves on the Board of Directors of Lincoln Center, is a member of the Board of Overseers of Memorial Sloan-Kettering Cancer Center, a member of the Board of the National September 11 Memorial & Museum and a member of the Museum of American Finance's Advisory Board. $

1. More than 250 people attended the Museum's 2013 gala in January. **2.** (L to R) Chairman Richard Sylla, President David Cowen and trustees Myron Kandel and Timothy Schantz. **3.** (L to R) Director of Development Jeanne Baker Driscoll with trustee Consuelo Mack and Museum founder John E. Herzog. **4.** Duncan Niederaur, CEO of NYSE Euronext. **5.** Bill Harrison, former Chairman and CEO of JPMorgan Chase and recipient of the 2013 Whitehead Award. **6.** Bill Harrison and John C. Whitehead. **7.** Erskine Bowles introduces his life-long friend, Bill Harrison.

1

MAY 11 1973 The Depository Trust Co. is established to smooth the delivery of securities and to provide a centralized electronic safety deposit box for stocks and bonds.

MAY 1 1975 Wall Street cries "May Day," as brokerage commission rates are deregulated by the US Securities & Exchange Commission.

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Photos: Elsa Ruiz

APR 18 1906

An earthquake levels San Francisco. Bank of Italy founder AP Giannini rummages through the rubble of his bank, retrieves $2 million in gold, coins and securities, and reopens for business on the docks near North Beach. The Bank of Italy later becomes Bank of America.

MAY 14 1884

The Panic of 1884 hits as railroad stocks crash amid price competition and excess capacity. Losses are estimated at $240 million.

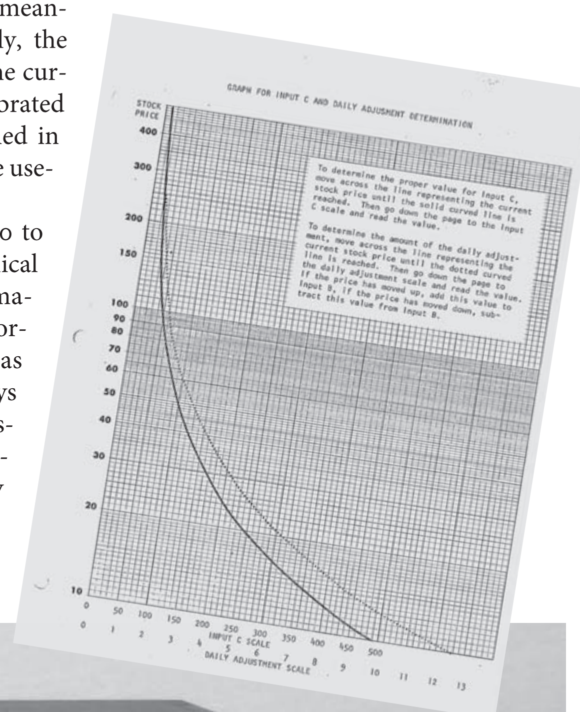
Museum Adds ISEC 250 to Financial Technology Collection

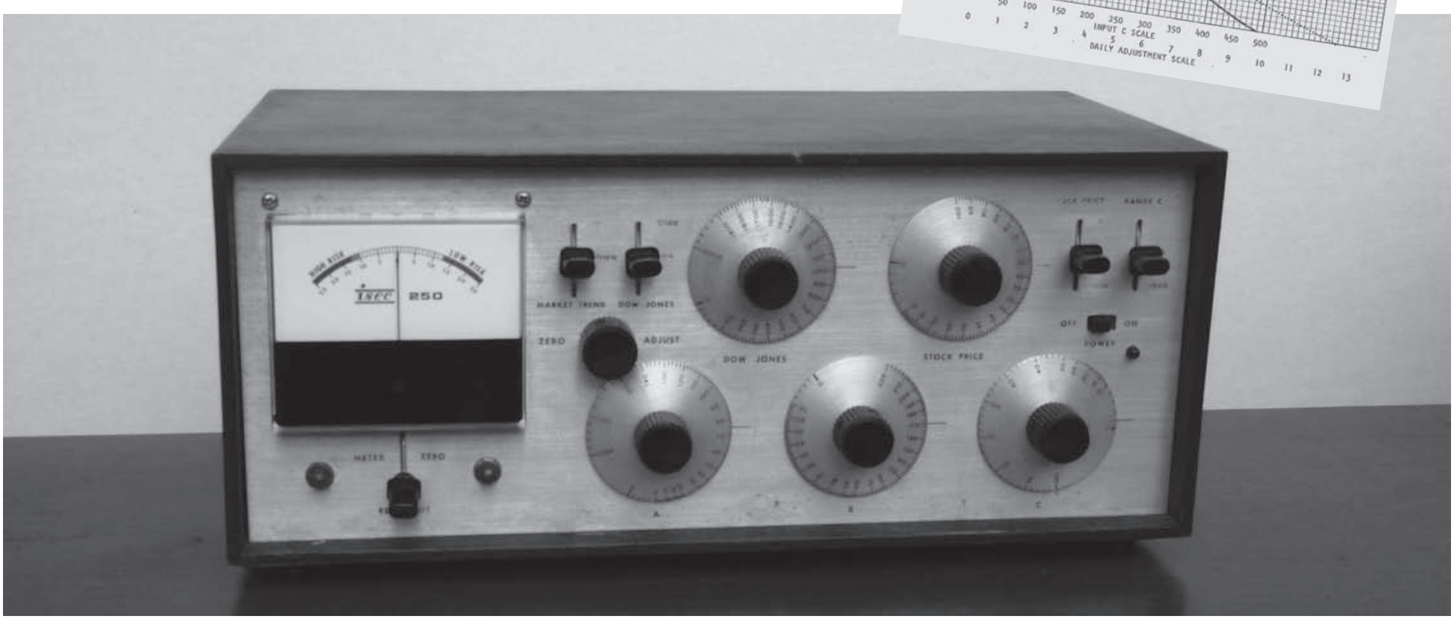
By Becky Laughner,
Director of Exhibits and Archives

The Museum staff is excited about a piece of old technology recently added to the collection, an early solid-state analog computer used for home investment analysis called the ISEC 250. The ISEC Corporation of Princeton, NJ, began manufacturing the machine around 1967 to assist hobbyist traders at home. The early computer is encased in wood paneling, covered in knobs and switches instead of a screen and bears little resemblance to modern-day computers.

To operate the machine, users entered data on stock prices, market volatility and trends via its knobs and switches. Using pre-programmed functions to analyze the market, the ISEC 250 would determine whether optimal market conditions existed to buy the 2,100 securities pre-loaded into the computer. According to its manual, it could "…correlate investment information resulting in a meaningful stock evaluation." Amusingly, the computer required users to input the current DJIA, which could only be calibrated to 2,000. This milestone was reached in January 1987, rendering the machine useless today.

The Museum added the ISEC 250 to its growing collection of mechanical and technological objects. Information technology represents an important topic in financial history, as the flow of information has always been essential to traders and investors. Even before electricity, traders would try to find an edge by employing carrier pigeons or runners to race information from ships arriving from oversees at port to the trading floor. The ISEC 250 represents another approach (albeit, a novelty





Becky Laughner

The ISEC 250 and a graph for daily adjustment of the machine printed in its manual.

MAY 16 1972 Economist Milton Friedman rings the opening bell at the Chicago Mercantile Exchange to inaugurate the world's first day of trading in foreign currency futures.

MAY 24 1688 The earliest known book on the stock market, Joseph Penso de la Vega's *Confusion de Confusiones,* appears.

one) for investors to attempt to gain an edge. The ISEC 250's manual reminds its users of this competition:

> It is at this depressing time that the people who know value will begin to buy stocks. By and large, these are the professionals. These men are good. They spend their entire working life studying the market, and they will buy low and sell high more consistently than an amateur. *They are your competition. Either you are going to lose money to them, or they are going to lose money to you.*

The Museum's technology collection contains objects from the earliest days of telegraphy and includes everything from early calculators, telegraph equipment, typewriters, tickers, telephones, Dictaphones, early trading computers and even the first handheld trading tablets used on trading floors in the 1990s. Several of these objects are currently on view in the permanent exhibition, "The Financial Markets," and additional examples are on view on the Museum's lower level.

The ISEC 250 represents a unique piece of American financial history. If any of our readers have experience with this object, we would enjoy hearing your stories. $

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The Museum is most grateful for the support of the following major donors who have generously provided funding for the Museum in the past year.

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MAY 26 1983 Daily trading volume on the Nasdaq exceeds the volume on the NYSE for the first time ever, at 79,747,400 shares.

MAY 27 1933 President Franklin D. Roosevelt signs into law the Securities Act of 1933, requiring all issuers of stocks and bonds to publish a prospectus disclosing risks, conflicts of interest and ownership positions.

William Andrews Clark and the War of the Copper Kings

By Brian Grinder and Dan Cooper

While I am willing to waive moral rank and associate with the moderately criminal among the Senators… I have to draw the line at Clark of Montana. He is said to have bought legislatures and judges as other men buy food and raiment. By his example he has so excused and so sweetened corruption that in Montana it no longer has an offensive smell. His history is known to everybody; he is as rotten a human being as can be found anywhere under the flag; he is a shame to the American nation, and no one has helped to send him to the Senate who did not know that his proper place was the penitentiary, with a ball and chain on his legs. To my mind, he is the most disgusting creature that the republic has produced since Tweed's time.

— Mark Twain

William Andrews Clark and Marcus Daly did not like each other. If they had just been crotchety neighbors, no one would have cared about their feud, but since they were two of the most powerful businessmen in Montana, their disagreements boiled over into the realms of politics and economics and even reached into the halls of the United States Senate. What became known as the "War of the Copper Kings" would eventually bring Montana to the brink of economic disaster and tarnish its political image for decades. Although the original cause of the feud has been lost to history, it may have started innocently enough when Clark enjoyed some barbequed beef on a Friday in the fall of 1888 while he was campaigning to become Montana's territorial delegate to Congress.

Clark was initially attracted to Montana during the gold rush of 1863, when he and a partner left the gold fields of Colorado to mine a claim near Bannack, MT. Although a year of mining netted Clark about $1,500, he realized he could spare himself the arduous labor of placer mining and make more money by freighting goods to the mining camps. According to historian Michael Malone, Clark had "an uncanny knack for delivering the right commodities to the right place at the right time."

In 1872, Clark moved to Deer Lodge, MT, and became president of the newly-established First National Bank of Deer Lodge. An important part of the bank's business involved purchasing gold dust from local miners and reselling it in New York. Initially this was a profitable endeavor that netted about $150,000 per year but, more importantly, it introduced Clark to the financial establishment in New York.

Clark got back into mining in the summer of 1872, when he invested in four mines in the Butte area. He then spent the winter of 1872–73 studying metallurgy at the Colombia College of Mines in New York. By then Clark was prepared to offer the nation's young mining industry adequate levels of capital and excellent management. In return, the mines of Montana, Idaho, Utah, New Mexico and especially Arizona would make him one of the richest men in the world.

Meanwhile, a scrappy Irishman by the name of Marcus Daly was tapping financial resources from California in order to invest in what became known as "the richest hill on earth." The Anaconda Hill in the center of the Butte mining district contained enormous amounts of copper and would become the primary asset of Daly's Anaconda Copper Company. At first Butte seemed to be large enough to accommodate two oversized egos. The mining community was unique in Montana because the promise of riches attracted individuals from a variety of ethnic backgrounds. For instance, Daly was an Irish Catholic who preferred to hire his fellow Irish. Clark, on the other hand, was a Scotch-Irish Presbyterian with a penchant for hiring Cornish miners. Occasional tensions erupted between different ethnic groups, but for a mining town everyone got along fairly well — until the political bug bit William Clark.

Clark was hesitant to run for the office of delegate to Congress in 1888, but after winning a unanimous nomination, he thought he would be a shoo-in as a Democrat in a state dominated by Democrats. His Republican opponent, Thomas Carter, was a largely-unknown Helena lawyer whose only asset was his Irish heritage. Although Clark was an astute businessman, his personality was not conducive to politics. A less-than-flattering 1909 description of Clark claimed, "his heart is frozen and his instincts are those of a fox; there is craft in his stereotyped smile and icicles in his handshake. He is about as magnetic as last year's bird's nest."

However, the support of the Democratic Party and Clark's huge personal fortune should have outweighed his flawed personality. But the Irish Democrats voted for Carter, who won the election. An outraged Clark wrote, "The conspiracy was a gigantic one, well-planned and well carried out, even though it did involve the violation of some of the most sacred confidences…" He laid the blame for his defeat squarely on Marcus Daly.

Daly likely played a role in Clark's defeat, but Clark's own insensitivity to the Irish voting block caused problems for Clark's campaign. Historian David M. Emmons has identified at least two instances during Clark's campaign that

Library of Congress

Senator William A. Clark's Fifth Avenue mansion in New York.

upset the Irish. The first was during a speech in Missoula where Clark rather recklessly accused Patrick Ford of desertion during the Civil War. Ford was the editor of the *Irish World and American Industrial Liberator,* an Irish nationalist newspaper that was widely read by Irish immigrants to the United States — Marcus Daly included. Ford quickly and vigorously rebutted Clark's charge in the pages of the *Irish World,* but Clark never apologized for his remarks.

The second instance was the infamous barbeque mentioned previously. Emmons writes, Clark "scheduled a beef barbeque on a Friday, effectively barring Irish Catholic participation, then compounded his blunder by inviting the virulently anti-Catholic Patriotic Order, Sons of America, to attend." Others have offered economic explanations for Daly's defection to Carter, but such blatant cultural insensitivity in a political campaign has been enough to sink the hopes of many a candidate.

When Montana became a state in 1889, Clark was determined to win a Senate seat. At the time, senators were elected by the state legislature, but the Montana legislature, evenly split between Republicans and Democrats, could not reach a decision. The issue was resolved by each party selecting two senators and sending four men to Washington where the US Senate would decide the issue. Clark, who was one of the senators selected by the Democrats, went to Washington and watched from the gallery as the Republicans won a close vote that sent Clark and fellow Democrat Martin Maginnis home.

Clark, more determined than ever to win a Senate seat, ran again in 1893 but was defeated when the Daly Democrats in the legislature refused to vote for him. By 1899, Clark was desperate to win a Senate seat. In the 1893 contest, Clark had bribed a number of Republicans to vote for him, but in 1899 Clark's money deluged Montana legislators in a blatant attempt to buy the seat. Clark won in 1899 and once again headed to Washington, but the Senate refused to seat him because Daly's forces in Washington accused Clark of bribing state legislators in order to win the seat.

A committee chaired by Senator William Eaton Chandler of New Hampshire was convened to investigate the charges. Both Clark and Daly testified before the committee, which in the end determined that Clark's selection was null and void. A disgraced Clark was again forced to leave Washington, but he would return.

In 1900, Daly was dying of heart failure. He had sold the Anaconda Copper Company to the Rockefeller group who planned to buy out all of the other mining companies in Butte and consolidate everything into the Amalgamated Copper Company. Clark, still desiring a Senate seat, teamed up with upstart mining entrepreneur F. Augustus Heinze to do battle with the Rockefeller Empire. The campaign was successful, and Clark was legitimately elected to the Senate. In 1902, Clark made peace with the Rockefellers and eventually sold most of his Butte mining properties to Amalagamated. Heinze, however, kept up the fight and so irritated the Rockefeller crowd that they shut down all of their Montana operations in October 1903 and refused to reopen them until the state legislature conceded to their demands.

The shutdown brought Montana's economy to a halt for about a month. When the governor announced a special

legislative session to convene in December, the company began to reopen its facilities. The powerful Rockefeller forces were granted everything they had asked for in the legislative session, and Heinze went down in defeat.

Clark, meanwhile, served out his term in the Senate and did not run for reelection. He moved to New York and built a Fifth Avenue mansion that was, according to historian Richard H. Peterson, "so flamboyant and garish as to incite indignation and ridicule even in an age inured to such extravagance."

Clark died in 1925 at the age of 86. His fortune at the time of his death was estimated at $200 million. Perhaps Malone said it best when he observed, "So long as he kept to business W.A. Clark always excelled. His problems persistently arose when his social-political pretensions and his urge to flaunt his wealth got the best of him." Had he stuck to his core competencies, Clark may well have been remembered as one of America's most successful businessmen. $

Dr. Dan Cooper is the president of Active Learning Technologies. Brian Grinder is a professor at Eastern Washington University and a member of Financial History*'s editorial board.*

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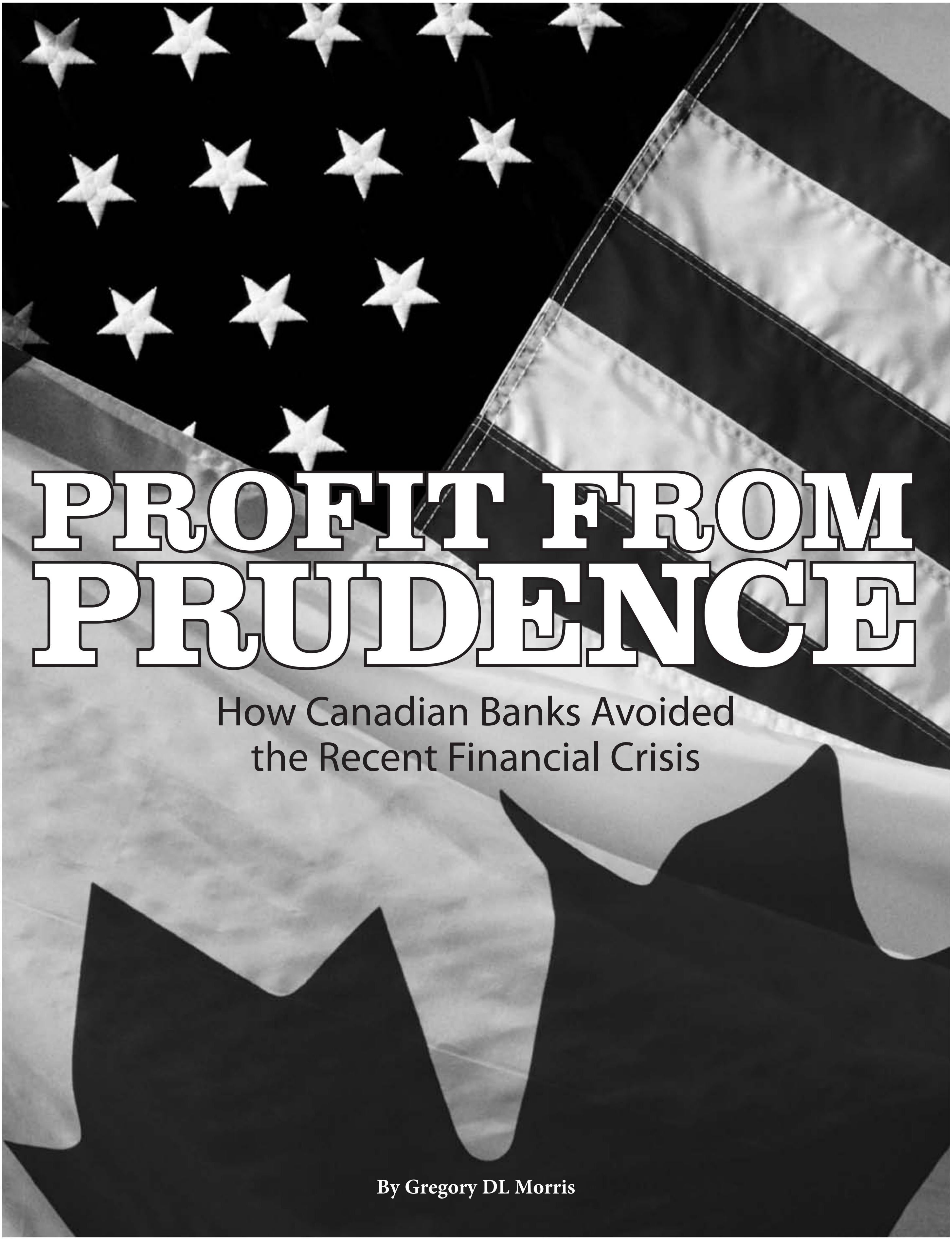

PROFIT FROM PRUDENCE

How Canadian Banks Avoided the Recent Financial Crisis

By Gregory DL Morris

While banks in the US and Europe faced existential risks in the financial crisis of 2007–2008, and many are still shaky, there was a reassuring quiet north of the 49th parallel. Like the dog that did not bark in the night in the Sherlock Holmes *Adventure of Silver Blaze,* the Canadian banking system was notable for what did not happen. There were no failures, no seizures for lack of liquidity and no collapse of the mortgage market. There was one brief crisis relating to asset-backed commercial paper, but the federal Office of the Superintendent of Financial Institutions (OSFI) acted quickly, and the problem was resolved in short order.

For two countries that are so intimately interconnected in finance, trade and language, the difference in regulation and risk management could not be more stark. And it is important to stress that the difference is not merely a function of Canada having about a tenth of the population of the US, or a largely resource-based economy. Often the distinctions between the US and Canada have been attributed to the disparate basic principles of the two countries. The US was founded on the ideals of life, liberty and the pursuit of happiness, while Canada was founded on the ideals of peace, order and good government.

Within the patriotic flourishes lie the kernels of truth. In the banking crisis, the biggest difference is most often attributed to the regulatory structure, both in its simplicity and in regulators' willingness to act swiftly. Don Drummond, former chief economist for TD Bank, and also former financial regulator, said he agrees the laws governing the financial system in Canada and the interaction between banks and regulators were factors. But he ascribes the true difference to prudence and sound risk management by the senior executives at the big national banks.

"Most people grab the government line that regulations and regulators were the difference," said Drummond, who is now a professor of economics at Queen's University in Kingston, Ontario. "Certainly the regulators did play a role, but the banks never ran to their regulatory capital or leverage limits. They were risk averse. They were profitable because they were prudent."

More than all the exposés of misdeeds by US bankers or lax oversight by US regulators, Drummond's assertion calls into question the very driving force behind the risks taken by US bankers: higher returns for higher risks. The 300-page report issued on March 14 by the US Congressional subcommittee investigating the $6.25 billion in trading losses by JPMorgan Chase, the so-called "London Whale" scandal, found that all the mischief was done in the name of big profits.

It is a classic manifestation of the tortoise and the hare; US banks were swinging for the fences and struck out, while the Canadian banks just kept hitting for percentage.

"If you look at the Basel recommendations for Tier 1 banks' capital ratios, it is 6%," says Drummond. "US and European banks all resisted that level, and in recent history have run ratios of 4–5%. Canadian banks are restricted to 7%, and yet none of them ever ran less than 10%. Same with leverage: Lehman was running 40:1. Canadian banks are limited to 22:1 and none ever ran worse that 18:1."

Drummond dismisses the disparagement that Canadian banks can afford to be more conservative because there is less competition. "Yes, there is an oligopoly of five big banks, but the risk aversion does not mean they have not been able to make incredible rates of return. The history of Canadian banks has been high and steady risk-adjusted profits. Typically they have made 20–27% return on equity without taking huge risks."

One of the major demons often cited for the meltdown in the US financial sector was the repeal of the Glass-Steagall Act of 1933, which separated investment banking from retail banking. That rule held for seven decades, but in 1999 Sanford Weill, chairman and CEO of Citigroup, led the charge to support the Financial Services Modernization Act, known as Gramm-Leach-Bliley, that broke the glass.

Citi alumni have since come to rue their championing of that cause. In April 2012, Citi Chairman Richard Parsons said in his valedictory address to shareholders at the annual meeting, "The 2007–2008 crash was the result of the throwing off of Glass-Steagall." And Sandy Weill himself said in an interview on CNBC in July 2012 that the major financial empires like the one he built should be dismantled.

Those policy debates are still raging, and too-big-to-fail remains a flashpoint, but Drummond notes that the big national Canadian banks have been involved in both wholesale and retail banking for decades, and it was no liability during the financial crisis. "All the big stand-alone brokerages in Canada were bought up by the banks in the late 1980s. As stand-alone operations, wholesale banking tends to make money nine out of 10 years, and then lose much of it all in that 10th year."

Having the two operations together under the same corporate roof is not inherently bad, Drummond argues. Indeed, the two can act as counterbalances. "Having the profitability of the wholesale banking is great in the good years, and having the safety and security of retail deposits and lending is great in the bad years. When the big Canadian banks started to acquire the wholesale banks, we originally set the target ratio at 60% retail to 40% wholesale. After a while we pushed that to 80:20."

This is not to say there was never any trouble. Indeed there was a test of retail and investment banking cohabitating. "CIBC got into some serious trouble," Drummond said, "and the wholesale banking group would have gone broke if it had been out on its own. It would have been another Lehman Brothers except for the strength of the deposit base."

Canada as a whole economy also went through its cycles. Peak to trough, Drummond said, the Canadian gross domestic product numbers were similar to those in the US. He said that with so many close correlations, the major factor that stands out is that his country did not have a housing crisis.

"Canada is the only major country worldwide that did not have a collapse in the real estate sector," said Drummond. "From 2006 through 2008 you saw housing values in the US drop by a third. While there were some local markets in Canada that had some dislocations, overall Canadian housing prices continued to go up. There was also no big drop in employment."

According to Drummond, one major reason there was no housing collapse is another stark tortoise-and-hare contrast

to the US. "Canadian banks kept most of their mortgages on their balance sheets. In 2007, just before the collapse, about 67% of US mortgages were securitized as compared to about 27% in Canada. Securitization is a stupid practice. When banks have those loans on their books, they have skin in the game. That adds to the security and safety of the system. Securitization was designed to spread risk, which is fine in theory. But I don't think they ever thought of systemic risk."

Drummond is not just speaking from the safe remove of academia. As recently as November 2012, Mark Zelmer, OSFI assistant superintendent, voiced many of the same ideas in his address to the Canadian Financial Services Insolvency Protection Forum in Toronto. In particular, Zelmer dismissed the idea that only simple banking rules are wise. He also emphasized the principle of sound risk management and prudence beyond what regulations dictate.

"Nobody argues with the objective of [international financial regulation such as] Basel III. But some observers claim we should scrap what they see as an unduly complex, opaque set of capital rules and replace them with simpler rules like the classic capital-asset leverage test. This would see regulatory capital requirements set as a function of the size of bank balance sheets or total assets — not as a function of bank risk-weighted exposures, be they on or off-balance sheet. I appreciate their concerns."

Zelmer also said that although risk models used by banks are very complex, they remain a crude simplification of reality. "The information needed to run those models is expensive to acquire. And, setting risk factors using past data can be akin to driving using only the rear-view mirror; especially if one is relying on short data samples," he said. "Clearly there is a risk that bankers and their regulators may become overly attached to complex risk models. If they are not careful, they could lose sight of the bigger picture needed to conduct proper risk management. Turning back the clock and scrapping all those fancy risk models in favor of simpler tests is not an option from OSFI's perspective. Basel capital rules are complex because internationally active banks are complex. They supply very sophisticated risk intermediation services to meet the needs of their clients in the economy and other parts of the financial system. And, they tend to look for ways to minimize capital requirements."

Zelmer then turned his attention to the separation of retail and investment banking. "The financial crisis has also sparked debate on whether there should be some separation between commercial and investment banking activities. This idea has its roots in a previous financial crisis, the Great Depression of the 1930s. That crisis led to the introduction of the Banking Act of 1933, commonly known as the Glass-Steagall Act, in the United States," he said. "The goal was to protect the core commercial banking system from distress elsewhere in the financial system in the wake of the 1929 stock market crash. Recent proposals in the wake of the latest financial crisis are not so draconian."

Zelmer added that the Dodd-Frank legislation will restrict US banks from engaging in proprietary trading through the "Volcker Rule." In Europe, the Vickers Commission in the UK and the Liikanen Panel in the EU have been proposed to limit the funding of investment banking activities by deposits backed by government safety nets. Proponents of these proposals claim that some separation between commercial and investment banking activities generates two types of financial stability benefits.

"First, it is thought to protect the core commercial banking system from losses in riskier investment banking activities. And, second, it may result in a better allocation of resources from a societal perspective by limiting the cross-subsidization of investment banking activities by commercial banking," Zelmer said.

Just two months before Zelmer delivered his address, Malcolm Knight, Canadian economist, banker and policymaker, published a comprehensive comparison of the US and Canadian banking systems in *The American Review of Canadian Studies* (Vol. 42, No. 3), a publication of the Association for Canadian Studies in the United States. In it, Knight traces the many strengths, as well as a few of the weaknesses, in the Canadian banking system back to the same Depression that gave the US Glass-Steagall and numerous other financial reforms, including federal deposit insurance.

With a note of irony Knight wrote, "Suspicion of the 'money trust' led US authorities to try to control consolidation in banking early on; in Canada bank consolidation was well underway by the turn of the 20th century." He added with emphasis that "not a single Canadian chartered bank or major insurance company failed" during the Depression.

Narrowing the focus he explained that, "In the US, excessive risk-taking by banks was widely seen as a trigger of the Great Depression. The key to mitigating banking risks is to address the dilemma that bank depositors want to be able to withdraw their funds on demand, whereas banks earn profits by lending for much longer periods with significant risk that the loans will not be fully repaid."

Knight details the growth of both US and Canadian banking and regulation, laying out how "by the eve of the financial crisis in mid-2007, succession revisions of the Bank Act had established a Canadian banking system that was *well-capitalized, not excessively interconnected or complex, closely supervised, generally conservatively managed and grounded on a stable nationwide funding base*." [Emphasis his.]

It has been argued in various forums and by many different advocates that risk taking is as American as apple pie. In the early 1970s, Canadian radio host Peter Gzowski held a contest to establish the Canadian analog to the expression "as American as…" The winning entry came from Heather Scott, a 17-year-old music student from British Columbia. It showed a wry sense of humor and perspicacity beyond her years. As debates rage today in Washington, DC seeking a new model for sound but profitable banking, the advocates might do well to heed Miss Scott's insight: "as Canadian as possible, under the circumstances." **$**

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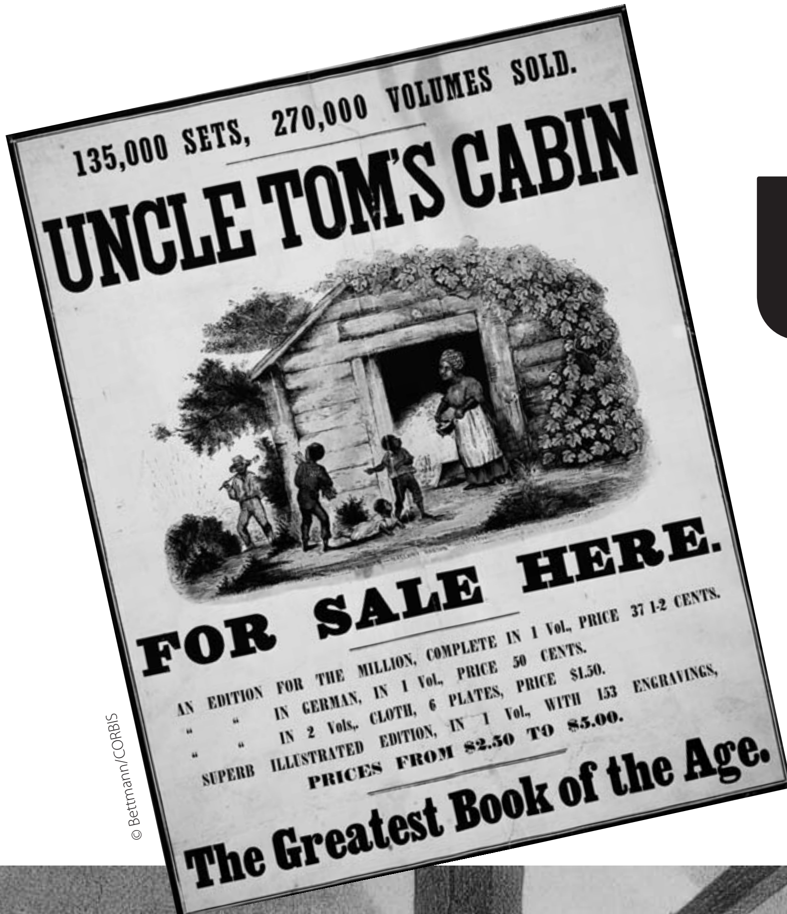
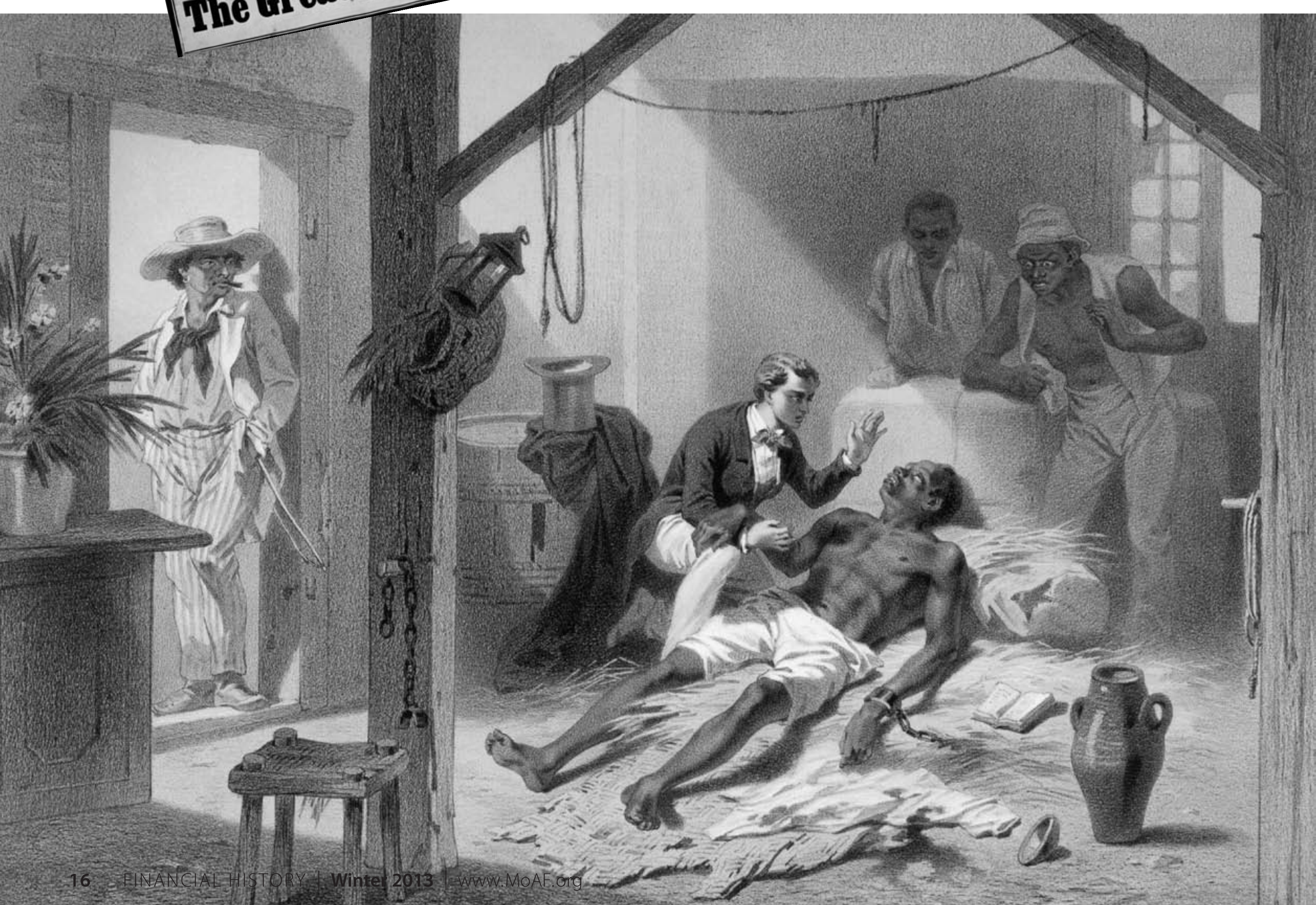
The Real **Uncle Tom** and the Unknown South He Helped Create

By Thomas Fleming





When President Abraham Lincoln met Harriet Beecher Stowe, author of *Uncle Tom's Cabin*, during the Civil War, he reportedly said: "So you're the little lady who started this great war." There was some truth to his words. The book played a huge role in persuading northerners to view southerners as cruel, corrupt and insatiably greedy.

Neither Lincoln nor the book's hundreds of thousands of readers had any idea that there was a real Uncle Tom and a real South that was very different from the portrait painted by Stowe and other anti-slavery critics such as her brother, the Rev. Henry Ward Beecher. Like Mrs. Stowe, most of these critics believed that God had inspired them to demand the immediate abolition of slavery—and condemn slave owners as contemptible. The vast majority of modern readers are equally unaware of the real Tom and the South he lived in.

The real Tom's name was Josiah Henson. He was born a slave in Maryland in 1789. Harriet Beecher Stowe admitted more than once that Henson's autobiography, published in 1849, was partly the inspiration for her novel. But she never explained why her fictional Uncle Tom was so different from the real one.

The difference was and is profound. The real Tom should prompt modern readers to reevaluate slavery's impact on American blacks. For too many decades the traditional story was something like this: slavery was a degrading, humiliating, demoralizing experience. Any black man or woman who endured it was reduced to subhuman status. They and their descendants, even when emancipated, would have to be treated like children at best—or creatures seething with a rage for revenge at worst.

Before and after the Civil War, this idea played no small part in poisoning the idea of black equality in the American public mind, North and South. In most northern states, before the war blacks could not vote, serve on juries or obtain decent jobs. They lived a segregated way of life in housing, schools and even churches.

Equally poisonous was the portrait of the southern economy and society that these critics of slavery created. The average southern planter was described as a dissolute wastrel who spent most of his time seducing his slaves. The non-slave holding whites were supposedly even more degraded. In time, these critics became paranoid believers in a myth they called "The Slave Power." They saw the South as a giant conspiracy which sought to inflict slavery and immorality on the entire nation.

In 1857, a North Carolina writer, Hinton Rowan Helper, published a book, *The Impending Crisis in the South,* which sold 150,000 copies. Helper claimed to base his gloomy predictions on census data and other hard facts, which proved the South was on the brink of economic collapse. Today we know the book was total nonsense.

The same can be said of *Uncle Tom's Cabin*, from a factual point of view. Mrs. Stowe never spent any serious time in the South. Almost everything she knew about the slave system was acquired from conversations with abolitionist relatives and friends. She made only two or three visits to nearby plantations during the 10 years she and her husband spent in Cincinnati, across the Ohio River from Kentucky.

To inspire outrage and pity, Mrs. Stowe portrayed her fictional Uncle Tom as an impossible mixture of competence and servility. She mentioned almost casually that he ran his master's plantation. But she never gave readers a glimpse of him at work. Instead she spent pages describing Tom as so kind-hearted he verged on a pathetic yes man who rarely, if ever, challenged his master's decisions.

Henson gives us a very different picture of the slave experience in his autobiography. When he was still in his teens, his master, Isaac Riley, began calling him "a smart fellow." His fellow blacks predicted he would do "great things" when he became a man. Soon he was vowing to "out-hoe, out-reap, out-husk, out-dance, out-everything every competitor." He did not hesitate to compete with white men as well as fellow slaves. He had a low opinion of the farm's sloppy and careless overseer. When he caught the man defrauding the master, Henson reported him.

Isaac Riley fired the thief and Henson asked for a chance to oversee the farm. He was soon raising "more than double the crops, with more cheerful and willing labor, than was ever seen on the estate before." Not only did Henson superintend the day-to-day work, he brought the harvested wheat and tobacco to market and bargained skillfully to bring home astonishing profits.

Stowe's Uncle Tom admired his incompetent master, even after he sold him to pay his bills. "Set him 'longside of other masrs—who's had the treatment and the livin' I've had?" he told his wife. The real Uncle Tom had no such high opinion of Riley. He was "coarse and vulgar in his habits, unprincipled and cruel in his general deportment." Riley sometimes cursed Henson for not getting a better price for a crop—and simultaneously boasted to friends about his new overseer's skill at the bargaining table. "He was quite incompetent to handle the business himself," Henson added.

At the age of 22, Henson married "a very well-taught girl, belonging to a neighboring family." By this time he had become a devout Christian, thanks to his mother's influence, and a white man named McKinney, who was a part-time preacher to local slaves. Henson's religion helped him put up with Riley. He considered it his duty to be "faithful to him in the position in which he placed me."

Henson was not some sort of mysterious exception to the rule in the slave world of the South. There were black men like him in every southern state. In South Carolina, William Ellison's master apprenticed him to a cotton gin maker. Ellison swiftly learned this technology and soon had enough money from repairing cotton gins to purchase his freedom and then the freedom of his wife and children. By 1860, he owned 1,000 acres of land and 63 slaves. He was one of the richest planters in the state.

By the 1850s, black overseers were far more common than most northerners of that era—and most Americans of the 21st century—have realized. Some historians

Top: Poster advertising *Uncle Tom's Cabin* as "The Greatest Book of the Age," 1859.
Bottom: Lithograph engraved by Charles Bour (1814–1881) of "The Death of Uncle Tom," from *Uncle Tom's Cabin.*

estimate that blacks predominated in that position on roughly 70% of the South's plantations that had 100 or more slaves. On smaller plantations, the overseer was almost always black.

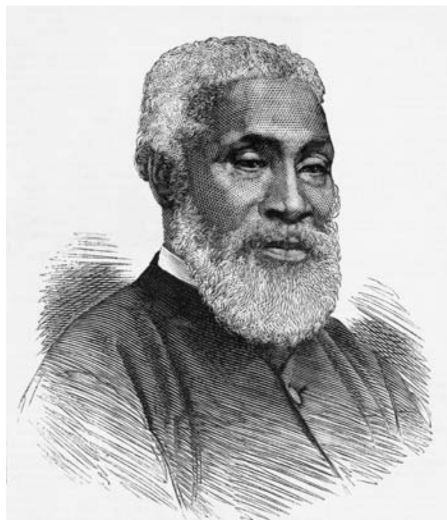
The importance of these black men can be glimpsed from a cry of distress from a Louisiana planter when his slave overseer died. "I have lost poor Leven, one of the most faithful blacks that ever lived. He was truth and honesty and without a fault that I ever discovered. He has overseen the plantation nearly three years, and has done better at it than any white man had ever done before…"

Managing a plantation was by no means the only goal to which a slave might aspire in the South — 27% of the adult male slaves in the city of Charleston were skilled artisans: blacksmiths, carpenters, coopers who operated as virtually free men. A slave plumber or shoemaker would and could advertise his services, negotiate his own contracts, receive and pay money and even live in his own house. His slave status required him to pay a percentage of his income to his owner. Otherwise, he was a relatively free man.

Slave artisans frequently made enough money to buy their freedom. In the 1850s, with the price of cotton soaring on the commodity exchanges, the price of a slave was high, perhaps $1,700 for a skilled worker like a blacksmith — the equivalent of $25,000 in modern dollars. That a black artisan could set aside this much money while paying his own living expenses and a portion to his owner is impressive. His slave status was in many ways more an artificial legality that a daily reality. The South's 260,000 free blacks were also far from penniless. They owned property estimated to be worth $25 million.

Even more surprising to modern readers is the number of slaves who worked in factories, displaying a gamut of industrial skills. The papers of David Ross, who operated the Oxford Ironworks in Campbell County, VA, one of the nation's largest factories in the pre-Civil War era, reveal that the business was staffed and run entirely by slaves. A man named Abram was responsible for the highly-technical and demanding day-to-day management of the blast furnace. The furnace keepers, Abram's chief assistants, had to know precisely how much charcoal and limestone to put into the furnace when it was in blast. All the other skilled workers — blacksmiths, potters, hammer men, miners — were slaves.

David Ross was proud of the many workers who had mastered more than one skill. His blacksmiths could double as potters and were adept at repairing or rebuilding the machinery of the forges, furnaces or mills. Of manager Abram, Ross wrote that he "supports an unblemished character, for his integrity, good understanding and talents." Like Henson, Abram had revealed these gifts virtually from his infancy, and still retained them in spite of his "gray hairs."



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Undated engraving of Reverend Josiah Henson, the original "Uncle Tom."

Once a white overseer of a nearby Ross farm complained that the owner had compared him unfavorably to Abram. Ross replied that the man must be mistaken. "It is hard to compare a farmer with an ironmaster." If Abram were a free man, Ross said, he would earn twice as much as the overseer, whether he was working in the North, South or West.

As the profitability of cotton culture rose in the 1850s, money became an ingredient in raising productivity on many plantations. Owners frequently paid between $40 and $110 a year — $600 and $1,650 in modern dollars — to experienced slaves for doing a good job. Slaves were also permitted to grow fruit and vegetables in their gardens and sell the produce. One industrious field hand made $309 in a single year selling peaches and apples on the side. In modern money that sum would be about $5,000.

In tobacco farming, where a high degree of skill was necessary, planters frequently paid slaves as much as $300 a year to guarantee a good performance. Rice cultivation required equal amounts of savvy. The plantations were divided into dozens of small watery plots surrounded by dikes. One traveler visited a rice farmer in Georgia and found a slave engineer who received "considerably higher wages" (in the form of presents) than the white overseer for his skill in building and maintaining the dikes.

On cotton plantations, the "gang" system required another group of leaders, who functioned as assistant overseers, somewhat like foremen in a factory or sergeants in an army. Before his gang went to work, the assistant overseer had to measure out their tasks for the day — no small job in fields that were often shaped irregularly. With a boy helper, the overseer would set stakes that usually covered about 40 acres, with the aid of a five foot measuring rod.

Once his gang went to work, the assistant overseer watched them closely to make sure they were not "overstrained." If he saw they were tiring, he had the authority to call a halt to the day's work. The next day he would order part of his gang to finish the previous day's assignment while the rest moved on to another section of the field.

Some planters, to increase productivity, entered into profit-sharing arrangements with their slaves. One Alabama owner permitted his bondsmen to keep two-thirds of the profits of the plantation, setting aside a third for his private use. From the slaves' share came the cost of clothing and food for them and their families, the taxes for the farm and medical bills. "What clear money you make shall be divided equally amongst you in a fair proportion agreeable to the services rendered by each hand," the contract stated. "Those that earn most shall have most."

These startling facts have come to light in the last three or four decades, thanks to research by a new generation of historians, who are trying to get beyond the myths about "the Slave Power" perpetrated by the abolitionists. Southern defenders of slavery also contributed to the myth by portraying black Americans as inferior in intelligence and ambition to whites and, thus, unable to handle freedom.

Perhaps the most startling fact these statistic-minded scholars have uncovered is the South's wealth. In the 1850s, the 15

slave states were by far the most prosperous section of the nation. Southern farms, many of them slave-managed, were between 35–50% more profitable than comparable farms in the free North and Midwest. In 1860, the South, considered as a separate country, would have ranked as the fourth richest nation in the world. Southern whites had a higher per capita income than citizens of France or Germany or Denmark.

Instead of pleasure-wallowing wastrels, most southern planters were hard-working businessmen who studied the latest techniques in scientific farming and did their best to keep their slaves contented in spite of the restrictions and confinements of the system.

A man who owned 50 slaves and managed them well with the help of a good overseer could clear $7,500 a year — the equivalent of $250,000 today. In the 1850s, this was 60 times the average white American's per capita income, North or South. The black slave overseer might get a bonus of $50 or $60 at the end of the year and a new suit. But he continued to live in a humble cabin in the slave quarters, starkly different from the master's "Big House." Worse, he was always in danger of being sold and separated from his wife and children.

Inevitably, this injustice bred resentment in black bondsmen. In addition to being classed as property, they were also cheated of a fair share of the profits from their labor. Historians estimate the average field worker was underpaid by $3,000 or $4,000 modern dollars annually. Overall, the South's slaves would have earned $84 million each year, if they had been given a fair share of the money they were making for their masters.

As property, the South's four million slaves were worth $3 billion. That sum exceeded the North's investment in railroads and factories. This figure does not include the value of the land that the South's farmers owned, which was worth at least another $3 billion.

If we study the income of those men who owned 20 slaves or more, which qualified them as "planters," some 46,274 individuals — a mere 00.58% of the South's population — the portrait is even more astonishing. These men owned half of all the slaves — which means, when combined with the value of their farms, their net worth was at least $1.5 billion. Put another way, they composed 70% of the richest people in the United States in 1860.

On a per capita basis, the four wealthiest states in the Union were South Carolina, Mississippi, Louisiana and Georgia. In the top 12 were only two northern states, Connecticut and Rhode Island. These newly-discovered facts demolish the standard 19th century assumption that the North was the dynamic section of the country and the slave-encumbered South was mired in backwardness and poverty.

"In the past, black men and women have been given almost no credit for the South's remarkable wealth. It is time to revise that mindset."

In the past, black men and women have been given almost no credit for the South's remarkable wealth. It is time to revise that mindset. The slaves participated in the system, not as mere automatons, but as achievers, frequently mastering the technology of the South's agriculture, as well as the psychology of leadership. A substantial number of black men and women did NOT succumb to the worst tendencies of the system. Their industrious lives within the unjust institution of slavery were a triumph of the human spirit over adversity that should no longer be overlooked.

These new facts about southern slavery not only contradict Hinton Rowan Helper's prediction of an imminent economic collapse, but they lead to a more interesting and possibly significant conclusion: slavery was evolving. Overall it remained a deplorable institution. But American freedom, sometimes disguised as business enterprise, was constantly seeping into the system. Would it have continued to move toward more and more freedom?

It seems inevitable that sooner rather than later, masters would have had to confront American slavery's greatest failure — its lack of freedom not only for gifted leaders like Josiah Henson and skilled artisans and factory managers like Abram — but for the children and grandchildren of such men. Slaves with above average intelligence and abilities found it harder and harder to tolerate a system which did not reward them adequately and condemned their descendants to the caprices of being sold to settle a dead master's estate or pay the debts of an incompetent owner.

Southerners were aware of this resentment. They had seen it explode into violent revolts more than once. In 1831, a charismatic preacher named Nat Turner inflamed blacks in Southampton County, VA, with a belief that God would protect their cause. In a 24-hour rampage, they killed over 60 white men, women and children. Thereafter, although southerners seldom admitted it to northerners, they lived with a constant fear of a race war, in which blacks would slaughter whites and vice versa, reducing the South to a blood-soaked shambles. This unspoken fear had long since become a disease in the southern public mind.

The angry abolitionists in the North refused to recognize this fear, and relentlessly demanded immediate emancipation, claiming God as their inspiration. They convinced themselves that they were rescuing whites as well as blacks from a failed and floundering way of life. Their contempt for southerners poisoned the noble side of their cause, making it another disease in the public mind. As the 1850s drew to a close, a perfect storm of deadly emotions was poised to engulf the United States of America. $

Thomas Fleming is an historian and author of more than 20 books, including several best-sellers. He has served as president of the Society of American Historians and the PEN American Center and also spent 10 years as chairman of the New York American Revolution Round Table.

BEGGAR THY NEIGHBOR

A History of Usury and Debt

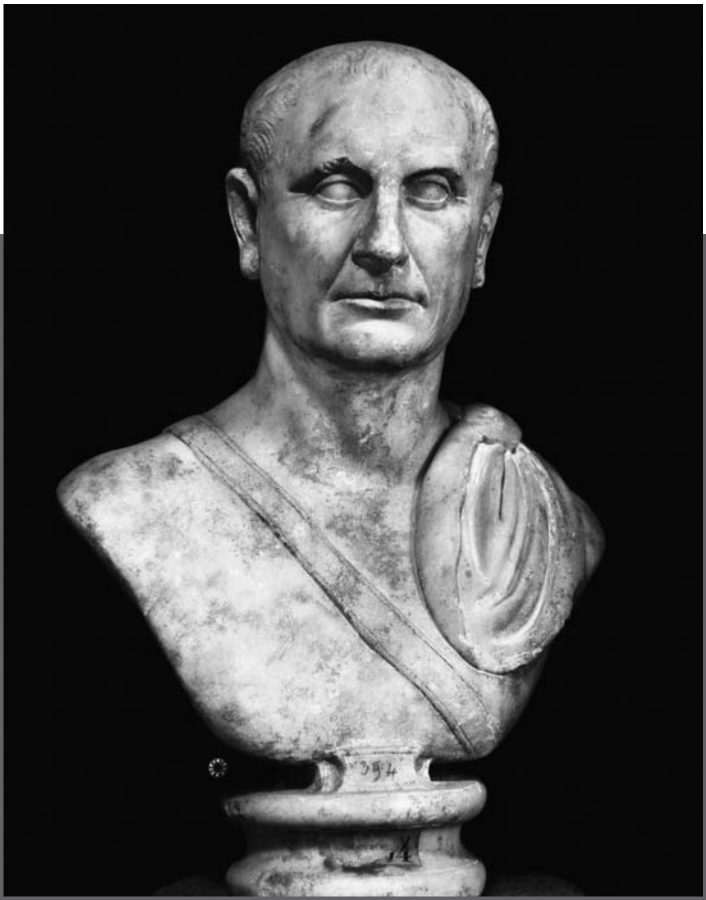
By Charles R. Geisst

Seven years before the assassination of Julius Caesar, an acrimonious dispute broke out between Marcus Tullius Cicero, at the time the provincial governor of Cilicia, and Marcus Junius Brutus, a young provincial Roman administrator. The elder statesman chided the younger man for using his administrative post in Cyprus to earn ill-gotten gains at the expense of the local people. Cicero received reports that Brutus had been lending money in Cyprus at four times the maximum rate stipulated by Roman law. To make matters even worse, he did it anonymously through an agent who did not mind using strong-arm tactics to collect the debts. When Cicero brought the matter to his attention, Brutus ignored him and continued to lend money. When he finally returned to Rome, he did so a wealthy man.

The problem caused Cicero to coin a name for the practice which became a cornerstone of Roman law. The story was told innumerable times over the next 1,800 years. The Roman historians dutifully recorded it, and Adam Smith alluded to it in the *Wealth of Nations*. According to Roman law, simple interest was permitted, but compound interest was anathema. Compounding had been used in many ancient civilizations, but the Romans eventually made it illegal. By doing so, they also established a tradition that would create much confusion in the centuries to follow. They did not make all interest illegal, only compound or "accumulating interest."

Prohibitions against excessive interest, or more properly usury, have been found in almost all societies since antiquity. Charging interest on loans is the oldest financial practice. It has also been decried almost from the beginning as predatory, with the lender seeking to take advantage of the borrower. Whether loans were made in cash or in kind, unscrupulous lenders were said to be practicing a beggar-thy-neighbor policy by ensuring that the borrowers were disadvantaged to the point of losing their collateral, or in extreme cases even losing their freedom or families. Charging simple interest was barely condoned, but charging compound interest was unscrupulous, immoral and rapacious. It was also practiced with near impunity.

The problem was clear in the ancient world but became obscured over time. Over the centuries, usury prohibitions



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Left: Bust of Marcus Tullius Cicero (106 – 43 BC), provincial governor of Cilicia, who accused Brutus of using his administrative post in Cyprus to earn ill-gotten gains at the expense of the local people through usury. *Right:* Statue bust of Marcus Junius Brutus (85 – 42 BC), who loaned money in Cyprus at four times the maximum rate stipulated by Roman law.

became part of civil law, and that unwritten law of nations generally referred to as the natural law. But it was still practiced widely and openly by the accursed moneylenders who quickly became part of legend and literature. This uneasy combination of theory and practice is partially responsible for the uneven patterns of economic development found in Europe from the decline of Rome to the Reformation. In the early Middle Ages especially, all interest was considered usury by the church. Compound interest became "Jewish interest," suggesting that it had dark, magical, non-Christian qualities that could be used for expropriation by the lender, considered a societal outsider.

Through its long history, interest and usury have gone from being anathema to being big business in the contemporary world, but they remain at least partially illegal in many jurisdictions. Many American states still retain laws against criminal interest, or loan-sharking. At the same time, it frequently is ignored in the same places with impunity and only becomes the center of attention in poor economic climates or in times of capital shortage or high inflation. Perhaps that is why it has remained part of the universal canon of proscribed practices.

Usury prohibitions firmly are part of the natural law tradition, in that natural law specifies what cannot be done. Since the fall of Rome, there have been more centuries characterized by what is known as capital shortage than there have been of periods of sustained growth and general prosperity. It is not a coincidence that the outcry against usury has been most shrill during those difficult times.

Today, usury is considered excessive interest, but that definition is relatively new in historical terms. Originally, *usura* was interest and its actual rate differed from place to place. The debate over it was intense. Excessive interest in many ancient societies was interest on interest, or *usurae usurarum,* which added to the principal of an unpaid loan. In the ancient world and Middle Ages especially, this was anathema. The tribal tradition of the Hebrews prohibiting Jews from lending to each other at interest was cited by medieval churchmen as the major Old Testament source for proscribing all interest, not just simple interest. The great irony was that Jews were exempt from lending to gentiles and accepted as moneylenders by the church in the Middle Ages. That loophole allowed them to compete with

the Lombards and Cahors who were allowed to lend at interest.

In medieval Europe, these groups were the main moneylenders before the arrival of the Jews. Curiously, none was condemned for it, and the Lombards were responsible for the development of the money markets in the 14th century. The Italian bankers in particular became financiers to monarchs and princes as far north as England. Their experiences with Edward III in particular were unpleasant, but their skills were highly sought after in countries where the treasuries were either low on cash or management skills. Despite the general ban on interest, the moneylenders were tolerated and even occasionally put the feet of monarchs to the fire when the interest bill was overdue. Jewish lenders usually were less fortunate. This apparent contradiction can be explained by a combination of tradition, religion and law. The Lombards were the barbarian tribe that conquered Rome in the sixth century; the Cahors were the descendants of the Visigoths who settled in France. Neither group had any provisions against interest or usury in their laws because both came from societies that originally used barter or payment in kind rather than money. Natural law in the late Roman Empire assumed a commonality among civilized societies, but that did not include barbarians. Neither group had a tradition against usury; each continued to pursue its newly-acquired money lending skills without interruption. No loud objection was heard until the Lombards were conquered by Charlemagne in 800, but by that time their tradition was established.

The barbarian invasions also relegated much of Roman law to the shadows of history until the general revival of learning in the 17th century. When many books that had been missing for centuries reappeared, those of Aristotle became the main reference for many churchmen, including Thomas Aquinas. This complicated matters for money lending because the Scholastics accepted Aristotle's dictum that money was sterile, having no intrinsic qualities other than being used as a medium of exchange. It could not beget itself, and therefore usury was not useful. Unknown (or ignored) was the discovery of Justinian's Code in 1130. In it, the prohibition against *anatocismus* (Cicero's term) and *alterum tantum* compound interest. Normal rates of interest were tolerated, but adding interest to outstanding principal was banned. But medieval church law would not even admit to ordinary interest despite the distinction between the two in Roman law.

Adam Smith, considered the father of free market economic theory, favored a ceiling on interest.

Compound interest would not become a math exercise until the Middle Ages, when the Italian mathematician Fibonacci discussed compound interest questions and puzzles. Because of the usury prohibition, he carefully avoided discussions about loan values and instead focused on future value problems, an issue medieval philosophers were not acquainted with and did not discuss. He posed questions about the future value of a unit of currency and, most famously, how many rabbits would be the result of an original pair, assuming continuous rabbit compounding. But he avoided the usury issue, as did his equally-famous countryman Luca Pacioli two centuries later when he discussed double entry bookkeeping. Fibonacci did, however, tackle the problem of debasing a currency, a politically correct topic in the 13th century for kings and princes.

There is a great temptation to criticize various usury and interest ceilings as being inconsistent over the centuries. The medieval church adopted a ban on usury, similar to the one in the Muslim world, only to see it circumvented with great frequency between the 12th and 19th centuries. Different commentators had sundry opinions on the subject, but all agreed that interest needed to be controlled. Even Adam Smith, considered the father of free market economic theory, favored a ceiling on interest. But as usury and interest approached the 19th century, it became more clear that there was a great deal of consistency in the way they were treated, given the differences in cultures and political motives of those opposed to them. The tendency to abuse one's position as a lender was recognized by most commentators regardless of their political or moral position.

The term "beggar thy neighbor" today is used to describe an international trade practice where one nation attempts to establish advantage over its trading partners through restrictive trade practices or policies. This derives from a mercantilist idea that owed its origins to an era when colonial powers exploited their far-flung colonies and ensured that they exported more than they imported. Before the mercantilist period, however, the term was associated more simply with borrowing and lending. The Shylocks of the world exploited the Antonios, seeking to extract their pound of flesh, when Christian principles demanded

fairness and lenient lending policies. Equity and Christian charity suggested that lenders should treat borrowers as brothers, members of the same community. The idea was practiced only rarely.

Shylock stood apart from that community; his religion and tradition were different; he was allowed to lend to non-Jews, a well-known, widely-circulated biblical fact. Coincidentally Portia, who successfully defended Antonio against Shylock in Shakespeare's court, was also the name of Brutus's second wife, which was probably not a coincidence since Shakespeare was well acquainted with Roman history.

The lending tradition became a nasty circle of recrimination and counter-recrimination that lasted for centuries. Lenders and early bankers, whether they were Jews, Lombards, Cahors or the Templars, realized that their financial expertise and alien status in many European societies made them subjects of envy, derision and ultimately retaliation from many hard-pressed sovereigns. As a result, many of them charged compound interest to compensate for their business risk or disguised interest charges as hidden, discounted fees. The risks they faced were more than simple counter-party risk because they could be expelled from their homes, sent to the Inquisition or expropriated. The fact that many well-known bankers in northern Europe prior to the Renaissance came from distant locales attests to the fact that foreigners were often sought as lenders precisely because borrowers could default on loans to them without much fear of reprisal.

The history of usury usually has been divided into a general discussion surrounding borrowing and lending on the one hand and the legal treatment of usury by various societies on the other. Since the early years of the Roman monarchy, through the republic and ending with the empire, Rome always had what is known as statutory usury. Laws governing interest were embodied in the law, at first in the *Twelve Tables* and then later in Justinian's *Code and Digest*. The latter incorporated the writings of many prominent rhetoricians and philosophers, so together they were an excellent compilation of the major ideas on usury in Rome for the previous centuries. These laws, different in scope and sophistication, actually specified the maximum rate of interest that lenders could charge borrowers. They did not ban lending rates but only sought a level of interest that was considered practical and viable.

To borrow an idea from Adam Smith, the more prosperous and wealthy a society, the lower its rate of interest. It has been suggested that the history of usury is nothing more than an exercise in intellectual history. Accordingly, usury is an idea with a long history, riddled with enigmas and inconsistencies, that exists mostly in the minds of economic historians. That is true, but it ignores the subtext, which has proved to be one of the most powerful notions in all societies for 3,000 years. As part of general natural law, it reflects societal notions of fairness and equity that have transcended ancient, medieval and modern societies. The power of interest, and especially compound interest, cannot be understated.

Usury and interest have been condemned together for centuries, although it is not always clear whether critics distinguished, or even understood, the differences between the two. Compound interest has commanded little discussion by itself until recently. John Maynard Keynes recognized the problems compound interest would cause for Germany in paying World War I reparations. Albert Einstein reputedly called it the eighth wonder of the world for its ability to produce future values far in excess of present value. The English clergyman Richard Price tried to use compound interest to retire the sizable British national debt in the 18th century. American lenders are now required to state the annual percentage rate they charge customers on unpaid balances, but the rates themselves have been left untouched by federal regulators. In the early 1980s, several large American banks went to great lengths and expense to establish credit card facilities in states with no functional usury laws in order to avoid potential prosecution for charging high interest rates, ratcheted even higher by daily or monthly compounding.

There has been a clear distinction between misgivings about usury and the law of usury. The misgivings certainly have been more colorful. Dante relegated usurers to the inferno while numerous writers cited scripture to illustrate the pitfalls of lending money. In early 19th-century Ireland, the Reverend Jeremiah O'Callaghan refused the sacraments to a dying man until he recanted his alleged usury, an incident that eventually got the priest banished to the wilds of northern Vermont. When the Catholic Church finally reconsidered its ban on usury, it did so quietly through a letter by the pope to the Italian bishops in the 18th century, not through a papal encyclical as would have been expected. One hundred years later, the ban would politely be ignored. After centuries of condemnation, the lure of fixed income investment returns finally became too great to resist.

Despite the colorful vignettes, it has always been easier to denounce the practice than actually pass a useful usury law. When the British government finally abolished its usury laws in the early 19th century, many of the arguments in the debate later surfaced in the United States. Banning usury was bad for business and, therefore, the usury laws should be abolished. No one could forcibly argue against the point, but no one could totally agree either, given the abuses to which lenders often subjected borrowers. Advocates of maintaining a ban often cited the Old Testament, and it became a major source of speech material for legislators in the 19th century.

While much of it sounded like hell, fire and brimstone, the laws that subsequently followed sounded very tame in comparison. Usury laws lived on in the United States for another 100 years. The fact that a major credit crisis followed within a few decades did not seem to faze proponents of leverage and free market interest rates who apparently were not aware that the South Sea Bubble, the Crash of 1929 and most of the American panics of the 19th and 20th centuries all were caused by excessive borrowing and high leverage that spilled over into the equities markets. **$**

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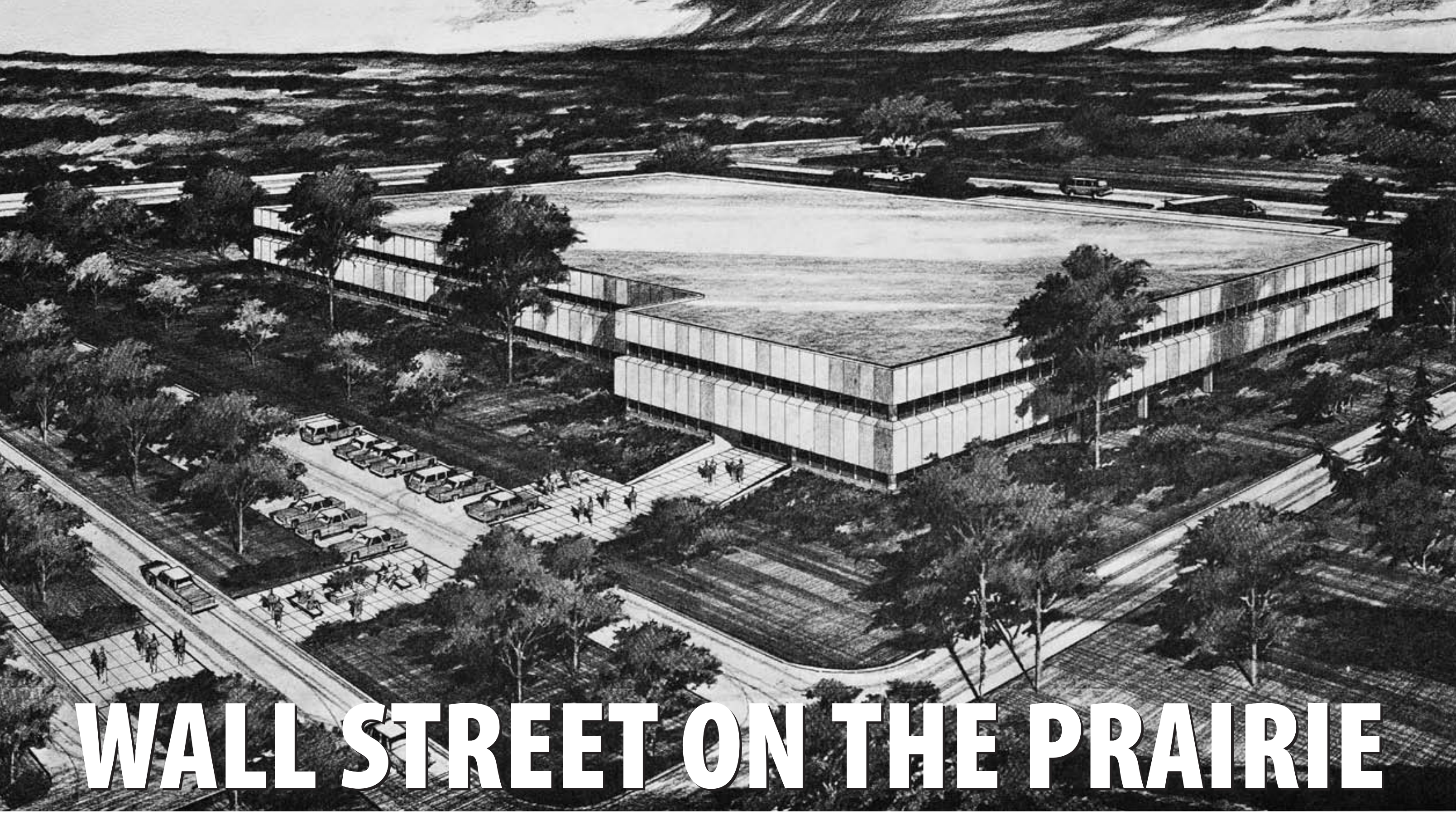

WALL STREET ON THE PRAIRIE

Citibank, South Dakota and the Origins of Financial Deregulation

By Robert E. Wright

"Homes across the land," *The New York Times* reported in the early 1980s, "are flooded with mailings from South Dakota offering … Mastercards—at a $20 annual fee and finance charges of 19.8%." How did a Great Plains state with a population smaller than many counties in the Northeast corridor come to export a cornucopia of consumer credit in addition to its usual superabundance of beef, hogs, small grains and other assorted agricultural staples? In the spirit of Enlightenment poet Alexander Pope's famous epitaph for Sir Isaac Newton: *Bill said, "Let Citibank come!" and all was plastic*.

The real story is, of course, more complex than that faux epitaph suggests. In early 1980, Citibank decided to relocate its massive credit card operations, which included some six million Mastercard and Visa accounts spread across all 50 states, to Sioux Falls, South Dakota's largest city. The Comptroller of the Currency approved Citibank's decision in November 1980, and the Federal Reserve did likewise in January 1981. Citibank South Dakota began operations in rented space in February 1981 and moved into the first of the three new buildings it would construct in the city that June.

Stunned by the sudden move, industry observers came to believe that Citibank had paid South Dakota to repeal its usury law, its cap on the rate that lenders could lawfully charge to borrowers. Although demonstrably false, the notion proliferated widely because it offered an easy explanation for Citibank's decision to invest in a state known more for harsh winters and impoverished Indian Reservations than financial acumen.

The myth of South Dakota's capitulation to the emerging megabank also made for great political satire, including an infamous fake news story that claimed that the South Dakota state legislature had voted to become a wholly-owned subsidiary of Citicorp. According to the faux article, the state was thenceforth to be called Dakotacorp, its iconoclastic Republican governor Bill Janklow was to be its highly-paid president and Pierre, South Dakota's capital, was to be renamed Wristonville after Citibank CEO Walter Wriston.

In fact, South Dakota's legislature moved to eliminate the state's usury cap before Citibank expressed any official interest in moving to Sioux Falls, and the giant New York bank moved to South Dakota for a number of valid business reasons, many of them unfathomable to those not conversant with socioeconomic conditions on the northern plains.

Foremost, South Dakota possessed an extremely favorable business climate. Janklow, its young, new governor, was eager to diversify the state economy, which was heavily reliant on farming in the east, ranching in its vast middle and mining and tourism in the Black Hills in its far west. He wanted to create more high-paying, environmentally-friendly jobs like those in Sioux Falls' burgeoning healthcare sector, and he rattled off the state's selling points to any corporate bigwig who would listen. South Dakota's overall business climate ranked 11th best

Rendering of the 118,000 square foot Citibank building in Sioux Falls, the centerpiece of its South Dakota Campus.

in the country at the time, and its employers enjoyed among the lowest rates for worker's compensation and unemployment insurance in the nation. The state was the first in the country to pass "right to work" laws. Not even its two largest industrial employers, Homestake Mining Company in the Black Hills or John Morrell's meatpacking plant in Sioux Falls, were unionized.

The state's tax burden was also very light, the 48th lowest in the nation. "In South Dakota," Janklow said, "the only hand in your pocket is your own." The governor also loved to tell prospective business entrants that South Dakota was the 50th best state in the nation: for crime, energy costs and time lost due to union work stoppages.

"South Dakota," one of his cabinet members added, "is a state where profit is not a bad word and where government views itself as a partner of business, not its regulatory master." Best of all, Janklow told skeptics, the state's pro-business climate was not a passing political fad but rather almost genetically ingrained in the electorate. "Republicans and Democrats have come and gone," he said, "but our 'business climate' has never been affected by the 'political weather.'"

Ultimately, the state's pro-business climate, not Citibank, was responsible for the repeal of its usury law. The 1970s had not been kind to the nation's banks, and South Dakota's were no exception. Stagflation, or high rates of inflation coupled with anemic economic growth, caused default and interest rates to soar while simultaneously destroying banks' gross spread, or the difference between what they paid for money and what they could charge their borrowers. The Federal Reserve's pro-cyclical monetary policies were the root cause of the stagflation, and the main cause of the deterioration of the margins were antiquated banking regulations enacted decades before inflation became a problem. Fed Reg Q capped the interest that banks could pay on deposits at rates far below those paid by money market mutual funds, so depositors pulled their money out, forcing banks to fund their loans by borrowing from institutional investors at high market rates. At the same time, state usury laws prevented banks from lending at the prevailing market rates. In other words, regulations and macroeconomic conditions essentially forced banks to borrow high and lend low, a losing proposition even before factoring in operating costs and defaults.

The crisis came to a head in late 1979 when Paul Volcker, the Federal Reserve's new chairman, raised the Fed's overnight lending rates in order to wring inflation expectations out of the economy. The resulting strain on gross spreads was more than most of South Dakota's banks could handle. Paul H. Nordstrom, president of the Security State Bank in Geddes, informed Janklow in late October 1979 that his bank could no longer afford to lend to anyone except a handful of its very largest and best customers. Janklow responded in early November that he agreed "that the interest ceiling in its present form is causing problems for citizens and our State-chartered financial institutions. This is the end product of years of federal, congressional and executive mismanagement and inflation. I can assure you that this problem will receive careful consideration during the forthcoming legislative session."

Citi's Center for Culture, Heritage Collection. Special thanks to Deb Larson, Citi South Dakota.

(L to R) Richard McCrossan, William Janklow and Charles Long celebrate Citi's 25th anniversary in South Dakota.

The legislature might have simply increased its usury ceiling a few percent to buy time as it and other states had done previously, but Thomas M. Reardon, the founder and chairman of Western Bank in Sioux Falls, and his son T.J. Reardon, the bank's president, had a better idea. They suggested doing away with the usury cap entirely for regulated institutions like their bank. South Dakota bankers quickly signed off on the radical idea and the lower house, which was dominated by libertarian-tinged Republicans, did too.

Meanwhile, Citibank's credit card division was hemorrhaging cash to the tune of $300,000 per day because it was paying 19% for money, lending it for less than that due to state usury laws, incurring operating expenses of 5–6% and suffering numerous defaults caused by the unsettled macroeconomic situation and the bank's own inability to discern good from bad credit risks. Rather than shutter the business, Citibank's Charlie Long, on orders from Wriston, began looking for a state with a more favorable business climate than New York had to offer. Pinning their hopes on the Supreme Court's 1978 Marquette decision, which allowed a bank to charge any rate of interest lawful in either its location or that of its borrowers, Long identified six prospects: California, Hawaii, Rhode Island, Nevada, Missouri and South Dakota.

Cinderella South Dakota won the contest. Once the state Senate learned of Citibank's interest in moving its credit card operations to Sioux Falls it passed the usury reform bill, which Janklow gleefully signed. The state then quickly moved on legislation inviting out-of-state bank holding companies into the state, a formality made necessary by the Douglas Amendment of the Bank Holding Company Act of 1956, which mandated that out-of-state banks had to be invited into a state before they could do business in it.

To get South Dakota state bankers on board with the idea of allowing huge potential competitors into their midst, the enabling legislation only allowed out-of-state bank holding companies like Citibank to form, own and operate in South Dakota small, new banks that did not compete against existing South Dakota banks. The state's bankers acquiesced, and the law passed with a large bipartisan majority.

Despite South Dakota's pro-business climate, Citibank's move still seemed dubious to many observers not conversant with the quantity and quality of the state's labor force and communication infrastructure. A credit card processing center needed to be well-connected to customers throughout the nation and, surprisingly, Sioux Falls was very well-connected indeed. For starters, its post office was so efficient that Janklow claimed, undoubtedly apocryphally, that a letter sent from one borough of Manhattan to another would arrive faster if sent via Sioux Falls rather than directly across the East River. What undoubtedly was true was that a

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Kenneth Francis Dewey

Published in *Fortune* magazine, this artwork depicts then-head of Citicorp, Walter Wriston, taking the place of Thomas Jefferson on Mount Rushmore. The drawing speaks to the impact the company had on the nation, and on South Dakota, in particular. November 21, 1983.

letter or check sent from most places in the country would arrive in Sioux Falls before it would in Manhattan. "It has been demonstrated," Richard C. Kane of Citicorp Credit Services wrote, "that the efficiency of the US Postal Service improves considerably when you are not dealing with major cities on either coast." By 1982, 32% of all the mail sent to Sioux Falls went to Citibank, but the local post office's performance did not suffer.

South Dakota was also well-connected to the national telephone network and to newer satellite communications technologies. Telephones (and automobiles) proliferated more quickly on the Great Plains than in more densely-populated areas of the nation due to the simple fact that they were more valuable to the denizens of remote locations than they were to city dwellers who had ample access to couriers and public transportation. Moreover, the federal government spent considerable sums ensuring that it could reach its important military assets in South Dakota, including the bomber base outside of Rapid City and the intercontinental ballistic missile silos peppered throughout the western part of the state.

South Dakota, therefore, had excellent, redundant communication systems, including "one of the most progressive telephone switching systems in the country." It was almost as fast and cheap for Citibank headquarters to call Sioux Falls as it was to call an uptown branch. Plus, Sioux Falls was in the central time zone, an hour behind Manhattan, but the same time as Minneapolis, Chicago, Kansas City, St. Louis and the rest of the densely-populated Mississippi basin, but just two hours ahead of California. Even more importantly, from most points in the country it was more expensive to pay for inbound customer toll free calls in New York than in Sioux Falls, which is near the east-west geographical center of the country.

Of course there had to be somebody in Sioux Falls to pick up the phone and monitor the mail, somebody who both needed a job and could adequately fulfill its duties. After World War II, the American heartland swarmed with simple, efficient gasoline-powered tractors, driving first horses and then men out of work. As tractors and their sundry attachments and cognates grew more complex, they also grew more expensive, creating economies of scale that spurred farm consolidation.

Then Jimmy Carter's grain embargo added to the general pressure by decreasing agricultural prices. In the early 1980s, therefore, South Dakota was awash in un- and under-employed men and women who had once been farmhands or even owned their own farms, or who had been teachers, shopkeepers or other types of service providers in the many little farm hamlets throughout the state that withered away as the rural population declined and the agricultural districts hollowed out. Many of those folks ended up in Sioux Falls and Rapid City, where they proved themselves a hard-working, dependable and intelligent labor force. South Dakota spent relatively little on K–12 education, but in the early 1980s the state boasted the highest literacy rate in the country, and a surprisingly large percentage of the population had college degrees.

Citibank was thrilled with the quality of the available workforce, which it considered the most productive of any in the 40 states in which it did business. South Dakotans worked hard, were naturally friendly and customer-service oriented, and had little discernible accent. They also came cheap. In 1980, South Dakota's per capita income was $7,800, 18% below the national average of $9,500. Unsurprisingly, the state's wage structure was low, healthcare costs were a third cheaper than in New York and rents were a fraction of those in and around Manhattan. Citibank has never regretted its move and, in fact, recently moved the nominal headquarters of its bank holding company from Nevada to Sioux Falls.

In the end, then, high wages, high taxes and injurious regulations pushed Citibank's credit card operations out of Manhattan while low wages and taxes, high productivity and high connectivity pulled it onto the prairie. The same dynamic pushed other credit card issuers into South Dakota as well, but other states soon caught on and began to loosen their usury caps, branching restrictions and other regulations as well.

South Dakota and Citibank countered by trying to subvert regulations banning the integration of commercial banks and insurers. Under the watchful eye of Paul Volcker, the Federal Reserve thwarted that attempt only to relax that and other prohibitions during the long chairmanship of Alan Greenspan. The result of that later wave of deregulation was disastrous, as the financial behemoths that resulted proved themselves too big to manage or govern and then too big to fail, but not too big to bail out with taxpayer money.

So while South Dakota gave financial deregulation a much-needed push in the early 1980s, it was not at all responsible for the excesses that led to the financial crisis of 2007–2009, which it weathered with remarkably little difficulty. $

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Library of Congress

Repudiation!

The Crisis of United States Civil War Debt, 1865–1870

By Franklin Noll

It was a time of unprecedented debt, of fears of austerity and of an unsettled currency system. It was 1865.

Emerging from four years of Civil War, the United States was faced with the task of reconstructing its political and economic systems. As part of this endeavor, from 1865 to 1870, much of the country's focus was on the massive public debt created during the conflict. Congress went so far as to pass a constitutional amendment that read in part, "The validity of the public debt of the United States … shall not be questioned."

Why was it necessary for the US Congress to alter the founding document of the nation to secure the public debt from repudiation? One might expect that in this time of upheaval the crisis was a financial one: the government, facing default, strove to force politics aside to resolve the situation. As it turns out, the opposite was true. The US was in no jeopardy of default, and the Constitution was amended to force politics into the economic equation for political ends.

The Civil War debt crisis actually consisted of three interrelated crises: a repudiation crisis, a repayment crisis and a refunding crisis. At the basis of all three was the battle for political advantage in the postwar United States. The Republican and Democratic Parties took concerns over the public debt and magnified them into crises. The resolution of the debt crises came only when there was no more to be gained from using the issue of the public debt for political advantage.

Secretary of the Treasury Hugh McCulloch successfully converted the nation's short-term debt into 6%, 20-year bonds by the end of 1867, averting a potential run on the Treasury.

What Crisis?

In the years 1865 to 1870, the ability of the US to pay its wartime debt never came into question despite its enormous size. The debt accumulated by the Union was unprecedented. During the war, the debt became 41 times larger than it was in 1860. The debt's peak was reached on August 31, 1865, with an outstanding balance of $2.8 billion. Not only was size a problem, but also the structure of the debt was far from desirable. The greenbacks, counted as part of the debt, fluctuated in value and saturated the money market. Meanwhile, short-term debt made up 48% of the total. This led to concerns that the Treasury could be caught short of cash as the instruments came due.

Despite these concerns, there was no panic that the country would be unable to meet its financial obligations. The US economy was essentially sound, and the tax system was "Spartan."[1] The people of the North also manifested a great impatience at the thought of indebtedness, and there was little actual pressure placed on Congress for tax reform. As a result, surpluses for the postwar years ranged from $927,000 to $116 million after making debt payments.

So, given the popular will for repaying the debt, the means to do so and the actual reduction of the debt almost annually, where was the crisis over the debt? In light of these facts, it seems there was no financial or economic crisis. Perhaps the crisis was one of confidence. Perhaps the question during the postwar years was not whether the debt *could* be paid, but whether it *should* be repaid—and, if so, how? Should it be paid in full? Who would bear the cost, and who would benefit? What happened to the public debt was an issue of profound importance to almost everyone dwelling in the North, not only because of the popular dread of indebtedness, but also because the debt itself was sacred.

The Sacred Debt

The economic magnitude of the public debt after the war was unprecedented, and so was the place it held in the popular psyche. The Civil War debt held a huge political charge in postwar America. This stemmed from the popular distribution of the debt and the way in which it was marketed.

Probably not since the Revolutionary War had so much of the public debt been held by the general public rather than financial institutions. The widespread distribution of US debt instruments resulted mainly from the Treasury's new dependence on popular support for its issues. Secretary of the Treasury Salmon P. Chase's financial inexperience led to numerous missteps in financing the war that earned

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Check drawn on Jay Cooke's bank. Cooke acted as an agent for the US Treasury and sold millions of dollars' worth of government bonds to small, novice investors.

him the distrust and hatred of the bankers and financiers of the major US markets. As a way to escape this situation, Chase turned to the idea of a popular loan, selling hundreds of millions of dollars' worth.

Most of these sales were conducted by the banker Jay Cooke as an agent for the Treasury. He focused on the small, novice investor. To win over these largely middle class buyers, his company advertised widely, laying out the financial benefit and patriotic significance of purchasing government bonds. Through these sales drives, the wartime debt became inextricably entwined with the patriotism and moral purpose of the Civil War. "Most … viewed the sanctity of the national debt as a moral legacy of the war second only to emancipation itself."[2]

However, there were fears that the need to pay the debt would lead to an austerity program that would increase taxes and throw people out of work. Following this train of thought, usually championed by the Democratic Party, the public debt was portrayed as a threat to the nation, particularly the lower classes. Taxation to pay for the debt, it was argued, would lead to an increasingly permanent and powerful class that derived its riches from government bonds, known as the "bondocracy."

Thus, at the end of the Civil War, the stage was set. There was a debt of unprecedented size and complexity, with much of it quickly coming due for payment. Much of this debt was held by a large number of middle class northern voters, many of them novice investors who saw the debt as a sacred legacy and feared for its safety. Yet, there were many from the lower classes who did not hold bonds and felt crushed by the heavy, regressive tax system used to pay the debt. These fears were expressed and exploited by the political parties of the postwar period in their struggle for power.

The Repudiation Crisis

The repudiation crisis was the fear that a politically resurgent South, represented by the Democratic Party, would force the government to repudiate the Union debt or force the repayment of the Confederate debt. Efforts to secure the repudiation of the latter began during the Civil War, but without success. After the war, President Andrew Johnson made it clear to a number of southern governors that they had to repudiate the Confederate debt as a condition to readmission to the US, but they balked at the idea, leaving matters unsettled.

There was also anxiety over the security of the nation's public debt. Representative Henry Winter Davis wrote, "None of the white population of the Southern States is interested in paying the public debt…. If the whites [Democrats] be restored to political power, their representatives are interested in repudiating that public debt."[3] The financial markets were nervous to the point that *The New York Times* had to repeatedly assure readers that the public debt was in no danger.

In May 1866, all the fears of repudiation were brought together into clause four of the 14th Amendment. It provided for the security of the public debt of the United States and repudiated the debt of the former Confederate States of America. However, section four was also widely seen as a political move to bolster the chances of passage of the entire amendment that included civil rights for former slaves and other controversial elements.

The *New York Herald* summed things up, saying: "Herein lies the secret of the astounding popular strength of [the 14th Amendment's debt clause] … No man who has a fifty dollar government bond salted down would trust its redemption to [a Southern, Democratic Congressman]."[4] Indeed, the threat of repudiation was seen as a vital political weapon by the

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President of the Confederacy Jefferson Davis confronts Brother Jonathan, who stumbles under the enormous burden of a bundle marked "Confederate Debt $650,000,000" and "Federal Debt $1,500,000,000" and is further weighed down by the figure of a black man in chains. Currier & Ives cartoon published in 1862.

Republican Party, which began to identify the Democrats with repudiation of the public debt.

The Congressional elections of 1866 resulted in a resounding success for the Republicans, thanks, in part, to the panic they started over a possible Democratic repudiation of the debt. The Republican victory also assured the ultimate ratification of the 14th Amendment and the end to any legitimate fear of the assumption of the Confederate debt or the outright repudiation of the Union war debt. However, the Republican Party continued to use the fear of repudiation to combat the Democrats.

The Repayment Crisis

The repayment crisis was the battle over whether a significant part of the public debt would be paid in gold or in greenbacks. During the war, the country went off the gold standard and issued its first fiat currency, the United States note, popularly known as the greenback. By the end of the war, greenbacks were trading at a discount to gold, and some advocated paying off the public debt in the devalued currency.

Greenbacks were originally meant to be a temporary measure. The country, it was believed, would return to the gold standard immediately after the war. Working under this assumption, when writing wartime legislation authorizing loans, Congress did not always take the trouble to explicitly state in what form of currency the principal of the loan would be payable. This was the case with the Five-Twenty bonds, which totaled $606 million, or over 27% of the public debt.

This lack of specificity came back to haunt the Treasury after the war when the repayment of the public debt became a controversial issue. On July 11, 1867, George Pendleton of Ohio, former Democratic candidate for vice president in 1864, gave a speech in which he proclaimed that it was only just that the debt be paid off using the devalued government currency the Republicans created. This position was dubbed the "Ohio Idea" by the popular press and used as a weapon by the Democratic Party in the 1868 presidential election. Republicans counterattacked by equating greenback repayment with repudiation.

With Ulysses S. Grant as its candidate, the Republican Party defeated the Democrats in the autumn elections. However, the outgoing Democratic President, Andrew Johnson, struck back in his annual message in which he called for a repudiation of the debt. Expanding upon Democratic Party rhetoric, he warned that the debt would lead to a new form of slavery wherein "The lenders [would become] the masters of the people." The solution to these injustices was to quickly pay off the debt by making interest payments not to the bondholders but to the Treasury to retire the debt. He concluded, "The lessons of the past admonish the lender that it is not well to be over anxious in exacting from the borrower rigid compliance with the letter of the bond."[5]

A week later, Grant was inaugurated as President. In his inauguration speech, he made clear that all talk of the "Ohio Idea" was over. Grant called Congress back into session, and the legislation needed to pay all bonds in gold was signed into law.

The Refunding Crisis

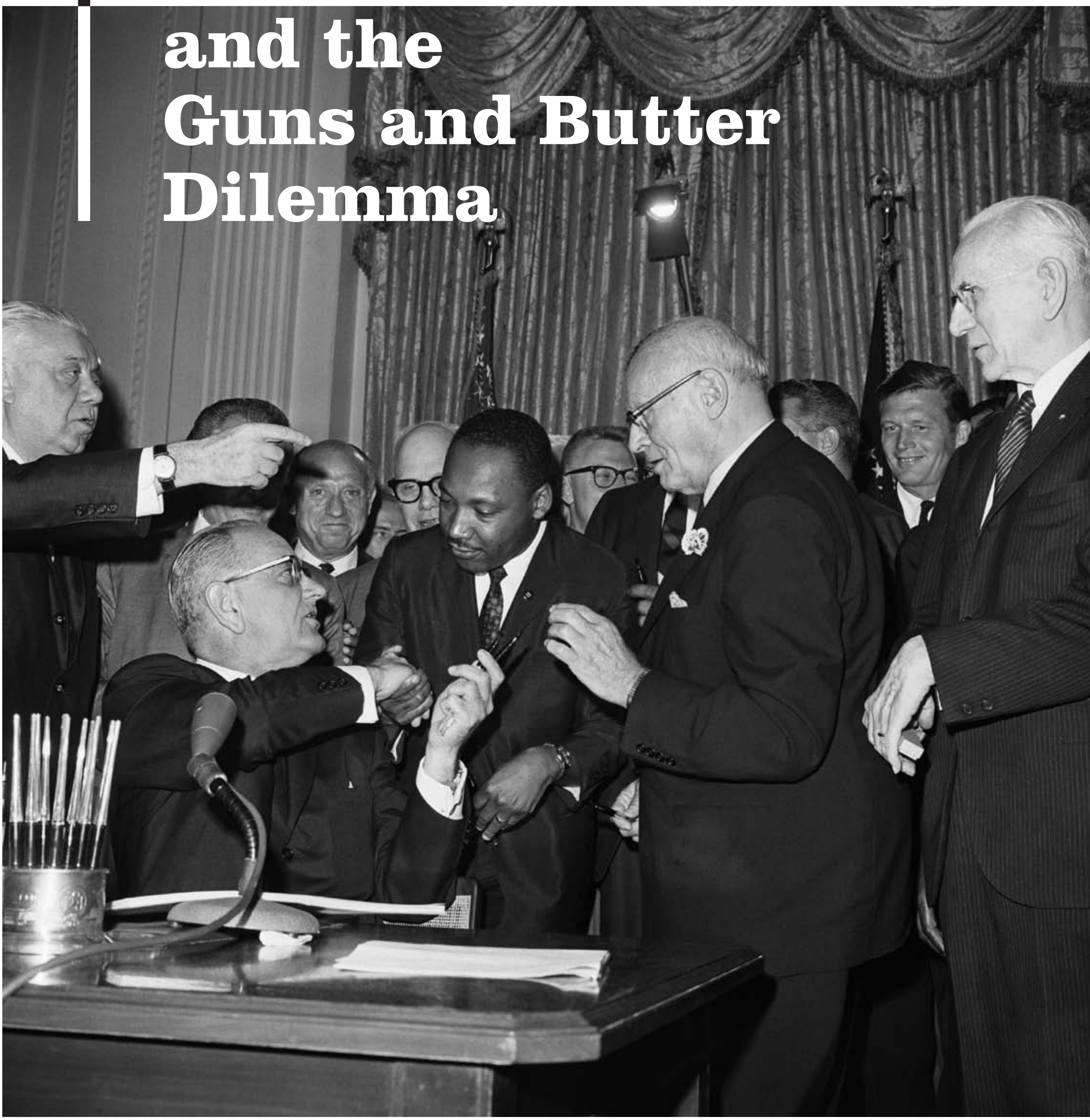
The refunding crisis was the pressing need to reorganize the debt's chaotic collection of high-interest securities, many of which were becoming payable. In fact, almost half of the debt would become payable by 1870. And, given all the debt that was subject to redemption by the holder on demand ($582 million or 22% of the public debt), there was a chance that the Treasury could be caught short of the funds necessary to meet the demand.

Secretary of the Treasury Hugh McCulloch believed all that could be done in terms of refunding was to consolidate maturing and short-term securities into long-run bonds at the high rates demanded by the market. By December 1867, McCulloch had successfully converted basically all of the debt payable on demand or short notice into 6%, 20-year bonds, averting a potential run on the Treasury. This achievement passed unnoticed as George Pendleton was touring the country at the time promoting the "Ohio Idea."

At the same time, Republican Senator John Sherman sought to force holders of Five-Twenties, paying 6%, to accept a 5% bond payable in gold. He thought this would be more attractive than the alternative, repayment in greenbacks. The bill passed Congress but fell victim to a veto by President Johnson.

» *continued on page 39*

Lyndon Johnson, Martin Luther King, Jr. and the Guns and Butter Dilemma



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President Lyndon Johnson shakes hands with civil rights leader Martin Luther King, Jr. and hands him a pen to sign the Civil Rights Act on July 2, 1964.

By Gary R. Hess and A. Dwayne Beggs

In the United States, wars traditionally have spelled the end of domestic reform. The American entry into World War I came after progressivism had achieved its major objectives. By the time the Pearl Harbor attack plunged the country into World War II, conservative opposition had largely stalemated Franklin Roosevelt's New Deal. The outbreak of the Korean War ended whatever prospects Harry Truman had to enact the Fair Deal.

The Vietnam War, however, was different. The year 1965 marked both the enactment of Great Society reform and the American intervention in Vietnam. Lyndon Johnson's reform was thriving just as he undertook a major military commitment.

Johnson's political career was driven by his determination to become a transformative leader in the tradition of Franklin Roosevelt. "My entire life, from boyhood on," he wrote in his memoirs, "had helped me recognize the work that needed to be done in America. My view of leadership had always been an activist one." In his first State of the Union address in January 1964, he declared an "unconditional war on poverty."

During his first year in office, Johnson concentrated on passage of the monumental Civil Rights Act of 1964. Then after his landslide election, using the formal and informal powers of his office with persistent effectiveness, he gained Congressional enactment of Medicare, the Model Cities Program, Operation Head Start and large-scale federal aid to education, housing and mass transportation — all in addition to the Voting Rights Act. Johnson thus had the building blocks in place for the Great Society.

Paralleling the enactment of the most ambitious domestic agenda in 30 years, Johnson faced a worsening crisis in Southeast Asia where the survival of the US-supported government of South Vietnam was threatened by a communist insurgency backed by North Vietnam. Gradually if reluctantly, Johnson Americanized the war. He began with a bombing campaign against North Vietnam, continued with the gradual introduction of American combat forces and concluded with a commitment to assure South Vietnam's survival.

In Johnson's political calculations, the crisis in Southeast Asia and the Great Society were interwoven. He feared the domestic consequences of "losing" Vietnam, believing that if the communists triumphed, he would be so crippled by conservative criticism that support for the Great Society would be lost. In his memoirs, he conceded that those domestic concerns drove the decision for war; he wrote that "the day that Vietnam became a matter of national debate, that day would be the beginning of the end of the Great Society."

The Great Society and the war were also connected in another way: the competition for resources. During the war's early months, it seemed to leading economists as well as many political leaders, including Johnson, that the economy was strong enough to finance "guns and butter."

Early in his presidency, Johnson had secured passage of the large tax cut proposed by President John F. Kennedy; individual tax rates were reduced by an average of 21% over two years and corporate rates by up to 48%. The tax reform generated by late 1965 a $25 billion increase in gross domestic product, reduced the unemployment rate to the historic low of 4.5%, produced an annual growth rate of 5.3% (compared to 2.5% in the 1950s) and maintained a low rate of inflation (1.5%). To blunt conservative criticism of "big" government spending, Johnson kept the federal budget below $100 billion annually.

Johnson's strategy of sustaining support for "guns and butter" through the stimulus of lower taxes, balanced budgets and low inflation — which reflected the consensus of liberal thinking at the time — soon unraveled. The unexpectedly high cost of waging war led him in January 1966 to propose an increase of $6.4 billion, with most ($5.8 billion) going to the war and some $600 million to the Great Society programs. With more than 200,000 troops on the ground in Vietnam, by March Johnson was requesting a $4.8 billion supplemental war appropriation, which increased the projected fiscal year deficit to $6.6 billion. Soon spiraling inflation and eroding investor confidence slowed economic growth.

Publicly Johnson maintained the "guns and butter" rhetoric. In his January 1967 State of the Union address, he called for expanding Social Security, Medicare, Head Start, Model Cities and anti-poverty programs in Appalachia. Privately Johnson recognized that this program was unrealistic at a time when the troop level reached 400,000 and the cost of war soared to $2.5 billion a month. Frustrated as he was by the failure to achieve victory on the battlefield, Johnson remained determined to maintain the prominence of the Great Society so that when the war ended, Congress would be committed to its fulfillment.

Up to that point, Johnson enjoyed the important support of Martin Luther King, Jr. Johnson's unequivocal support of civil rights legislation, after decades of presidential procrastination on the issue, solidified the backing of the nation's African American leadership; indeed, King was at Johnson's side when he signed the Civil Rights Act and Voting Rights Act into law. Johnson's dream of the "war on poverty" as the cornerstone of the Great Society further cemented his alliance with King.

King was not the typical political figure. He brought the prestige of moral leadership and enjoyed unique stature as the embodiment of the civil rights movement. His leadership through non-violent protest had earned worldwide recognition, most notably the 1964 Nobel Peace Prize. Although troubled to some extent by the US intervention in Vietnam from the beginning, King had put aside his doubts as he accepted Johnson's "guns and butter" assurances.

In April 1967, however, King broke ranks. In his "A Time to Break Silence" speech, he became an outspoken critic of the war. King's transition from deferential supporter of the war was gradual and agonizing, and it reflected a blend of moral, racial and political considerations. Over the course of the two years between the gradual Americanization of the war in early 1965 and King's "A Time to Break Silence" speech, he came to three interrelated convictions about the war: that it was immoral and his duty as a minister was to work for its end; that it was harmful to the African American community at home and on the battlefield; and that it was undermining the Great Society program.

From the beginning, Johnson's call for war troubled King. His early acquiescence concealed an inner conflict with his commitment to the principle of non-violence. King rejected absolute pacifism but considered war increasingly obsolete in the nuclear age. As he studied the historical context of the war and America's role in world affairs, King came to see Ho Chi Minh and other leaders of the "enemy" in Vietnam as principally nationalists, not part of an international communist

movement led by the Soviet Union and the People's Republic of China.

Missing an opportunity to work with Ho Chi Minh after World War II, the United States had supported France's ill-fated effort to re-colonize Vietnam. After France's defeat, the neo-colonial Americans had conspired with the ruthless Ngo Dinh Diem to create a dictatorial non-communist regime in South Vietnam. To King, the massive military intervention to save the unpopular South Vietnamese government represented the epitome of America's Cold War interventionism, which was directed against non-white people throughout the world.

King thus came to believe that the Vietnam War undermined both America's stature in the global community and the guarantees of racial and political equality in the US. To King, the Vietnam War was harmful to both the Great Society program and the African American community. In battle, African Americans were losing their lives at a disproportionate rate: they constituted about 10% of the population, but 30% of the war's casualties. As black troops fought to oppress other marginalized people of color in faraway lands, African Americans in the US suffered from continued inequality and the failed promises of Lyndon Johnson and the Great Society.

However strong his convictions, King recognized he was operating in a delicate political environment. His opposition to what was occurring in Vietnam would have a profound impact on various groups. It would provide a powerful voice to the anti-war movement and enhance its legitimacy. But it would also, of course, alienate Lyndon Johnson while enhancing the position of conservative members of Congress who would use King's new-found position to castigate the Great Society.

Reflecting the politics of the situation, King's initial criticisms of the war were relatively muted as he focused in 1966 on his Chicago protest against the slum conditions of the predominantly minority housing. In that protest, however, his rhetoric notably reflected his Vietnam-based broadened view of American racism. "The slum," he argued, "was nothing more than a domestic colony, where the few exploited the inhabitants who were segregated, humiliated and disempowered."

By the spring of 1967, King believed he had no alternative but to give priority to the war. Opponents of the war planned a Spring Mobilization with mass demonstrations in major cities. Historian Lloyd Gardner writes, "What the Johnson administration feared most came to pass. King was marching at the head of the movement."

Just before the Mobilization, speaking at the Riverside Church in New York City on April 4, King delivered "Beyond Vietnam: A Time to Break Silence" — arguably his most notable speech next to the "I Have a Dream" speech four years earlier. King spoke at length and with eloquence about his agonizing path to opposing "the madness of Vietnam." Speaking for the "suffering poor of Vietnam whose land is being laid waste, whose homes are being destroyed, whose culture is being subverted" and for "the poor of America who are paying the double price of smashed hopes at home and death and corruption in Vietnam," King proclaimed, "somehow this madness must cease."

King never mentioned Johnson, but he did not need to: his break with the President was unequivocal. In his most notable peroration, King underlined the war's devastating impact on America:

> There is at the outset a very obvious and almost facile connection between the war in Vietnam and the struggle I, and others, have been waging in America. A few years ago there was a shining moment in that struggle. It seemed as if there was a real promise of hope for the poor — both black and white — through the poverty program. There were experiments, hopes, new beginnings. Then came the buildup in Vietnam and I watched the program broken and eviscerated as if it were some idle plaything of a society gone mad on war, and I knew that America would never invest the necessary funds or energies in rehabilitation of its poor so long as adventures like Vietnam continued to draw men and skills and money like some demonic destructive suction tube. So I was increasingly compelled to see the war as an enemy of the poor and to attack it as such.

Johnson privately said that King had joined "the ranks of the crackpots and Viet-niks" and suspected that he was "on the payroll of Bobby Kennedy." To Johnson, King had joined the ranks of "all those liberals who don't appreciate all that I've done for them."

Despite Johnson's anger with King and other liberal critics of the war, it was a testimony to his convictions that he continued to pursue the Great Society. Increasingly, however, it became politically and fiscally impossible. Facing the politically-untenable $30 billion in deficits for FY 1968, Johnson proposed a surtax of 6% on personal and corporate tax rates. Soon it became evident that more revenue would be needed, so he increased the proposed surtax to 10%.

Congressman Wilbur Mills, chairman of the Ways and Means Committee, insisted on cuts in domestic programs in return for the surcharge. Johnson, besides being in the unusual position of not having the upper hand in negotiations with a congressional leader, encountered stiff public opposition as well: only 15% of Americans favored tax increases while 73% supported cuts in spending.

Salvaging the Great Society became enmeshed in a political struggle which was beyond Johnson's control. Liberals in Congress urged funding for reform and wanted to end the war and its drain on the American economy. Conservatives, including many Democrats like Mills, saw an opportunity to stagnate, if not kill, the Great Society and were determined to achieve victory in Vietnam. And outside Congress, anti-war critics, including King, hammered away at the ways the war continued to erode the Great Society.

It was not until June of 1968 that Congress finally passed the tax increase. The bargaining with Mills over spending cuts had begun at $2 billion; ultimately Johnson, by then a lame duck whose presidency was in shambles, had been forced to accept $6 billion. No longer did he talk about "guns and butter."

After he left the White House, an aging Lyndon Johnson reflected on the disappointments of his presidency. Mindful of how wars had impacted reform historically, he spoke with some bitterness of his experience:

> Oh, I could see it coming all right. History provided too many cases where the sound of the bugle put an immediate end to the hopes and dreams of the best reformers … Once the war began, then all those conservatives in the Congress would use it as a weapon against the Great Society … They'd use [the war] to say

they were against my programs, not because they were against the poor... but because the war had to come first. First, we had to beat those Godless Communists and then could worry about the homeless Americans… And I knew that if we let Communist aggression succeed in taking over South Vietnam, there would follow in this country an endless debate — a mean and destructive debate — that would shatter my presidency, kill my administration and damage our democracy.

Johnson never questioned that the nation could have afforded "guns and butter," and he never forgave those — including King — who found that promise to be beyond America's resources. $

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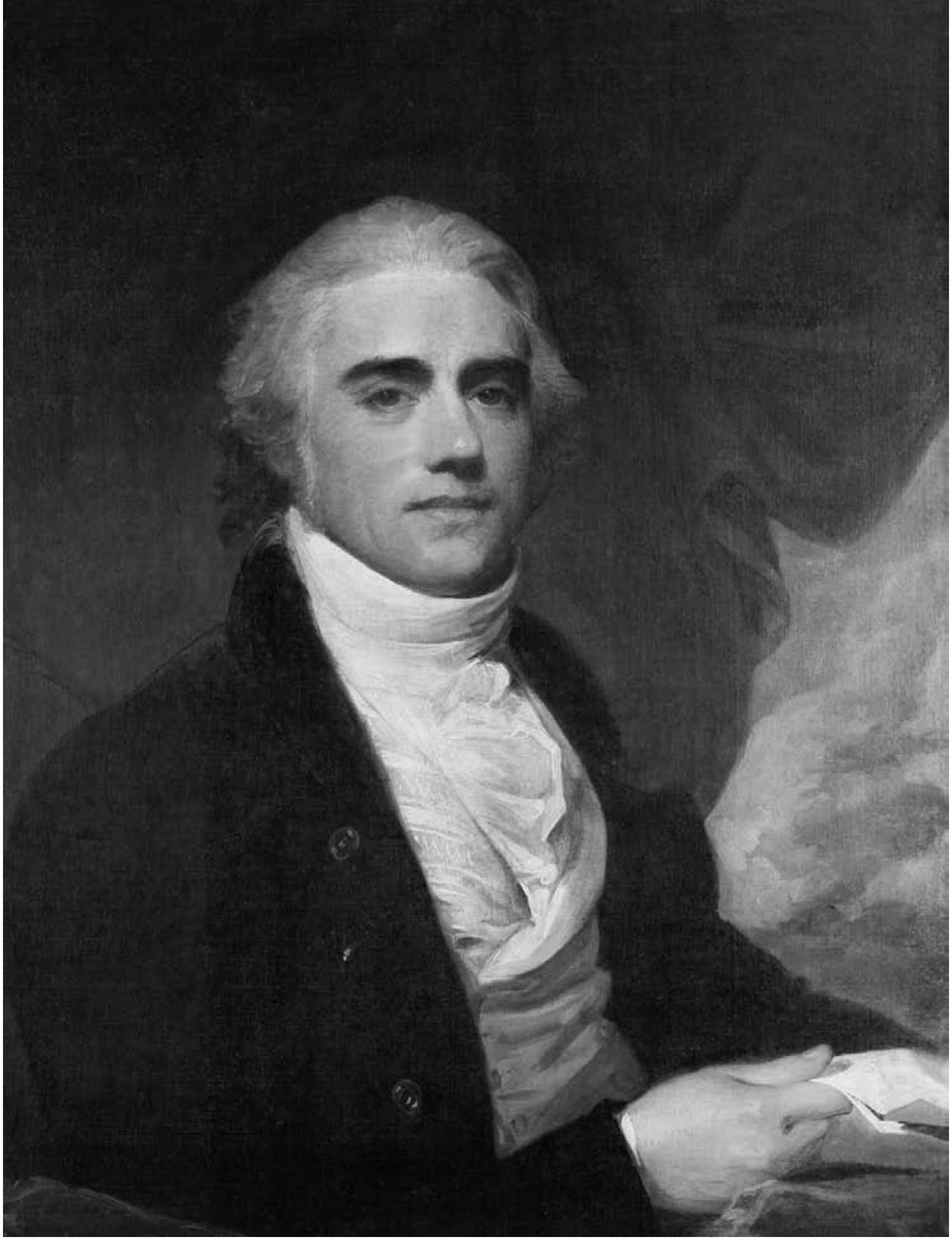


Samuel Meeker

MERCHANT OF PHILADELPHIA

The Gilbert Stuart portrait of Samuel Meeker [Philadelphia, 1803] reveals the sitter as a self-confident individual. His lightly-powdered hair with queue is in the style of George Washington, and his attire — consisting of a blue-black coat with brass buttons, high white neck cloth and ruffled shirt with striped grey satin waistcoat — indicates refinement. The business papers in Meeker's right hand reflect his profession as a merchant.

By Elizabeth Ahrens-Kley

To have one's portrait painted by the eminent American artist Gilbert Stuart (1755–1828) signaled arrival at the pinnacle of social and economic success. Famously described by First Lady Dolley Madison as being "all the rage," the artist was celebrated for his superlative portraits of Presidents Washington, Adams, Jefferson, Madison and Monroe. But who was Stuart subject Samuel Meeker, and how was he able to commission the foremost painter of his time?

Meeker was a scion of the famed Meeker family, participants in the founding of the state of New Jersey and long known as dedicated and ardent patriots. Progenitor William "Goodman" Meeker skirmished against the British governor in the 1670s; a relative, Major Samuel Meeker, sustained wounds in the Battle of Minisink in 1779; and his father, Captain Samuel Meeker, served in the Essex Troop of Light Horse, which paraded before General Washington. Samuel himself served as captain, and then colonel, of the Third Troop of Philadelphia Light Horse during the War of 1812.

Meeker's father had developed a prosperous career in timber and cabinet making in Elizabethtown, NJ. The tax tables of 1779 indicate that Captain Meeker was well-to-do, showing ownership of more than 130 acres of land, as well as horses, cattle and a riding chair (an expensive luxury, being one of the few items taxed in addition to livestock).

Samuel was raised in a world of long hours, hard work and risk. Although he had privileged beginnings, upon entering the mercantile trade, business was precarious and success was not guaranteed.

Opportunity abounded in the burgeoning business environment of Philadelphia at the turn of the 19th century. It was both the center of American commerce and the seat of the federal government, providing a fertile environment for business growth. A favorable location for trade by ship, distinguished politicians attending to government and wealthy emigrants escaping the political turmoil in France helped to bring urban consumerism to new highs in the city.

By many accounts a competitive and talented man with a driven personality, Meeker was propelled to extraordinary heights of risk-taking and bold

speculation. In addition, his known acts of charity, military service and civic activities inspired trust that was vital to the career of a successful merchant. As a merchant trader, insurance tycoon, banker and land investor, Meeker was both a dynamic participant in, and an engineer of, the surging economic development in post Revolutionary War America.

An Entrepreneurial Spirit and Maritime Insurance

The success of two Meeker firms in the 1790s enabled Samuel to build his reputation and increase his capital. His twin sister, Phoebe, married William Cochran, merchant at 34 Chestnut Street, in 1792, and Meeker and his brother-in-law formed a trading partnership, Meeker, Cochran, & Co., the following year. They invested funds in the transatlantic import of "dry goods," sold both from the firm's warehouse at 28 North Front Street and wholesaled to the hinterland. Andrew Jackson bought supplies from the company for his southern trading operations, and the firm dealt extensively with the US Department of War. By the mid-1790s, Meeker increasingly handled financial instruments, such as drafts and bills of exchange, particularly in association with the US government.

Meeker dissolved his partnership with Cochran in 1797, after Phoebe's divorce, and established another firm, Meeker, Denman & Co. Through this firm, he conducted business from Natchez to Cincinnati to Lexington, and he traded goods including cotton, tobacco, flour and pork. The company imported textiles, clothing, gloves, buttons, blankets and furniture from London and Liverpool and sold them from a warehouse on South Front Street.

In 1802 the *Pittsburgh Gazette* read: "sailed on Sunday east from this place for Liverpool, England, the brig "Dean" burthen 170 tons. She takes in a cargo of cotton at the mouth of the Cumberland River, on freight, by Messrs. Meeker, Denman & Co., merchants of Philadelphia." Meeker was also in contact with the federal government regarding concerns over US trading vessels, writing Secretary of State James Madison about British actions which had "totally suspended the commerce of the western country, and its produce, much of which is perishable, will be a total loss…"

By then the firm was conducting large capital transactions equivalent to banking functions; federal troops stationed in the new state of Tennessee for the protection of American citizens against Indian threats were paid through the auspices of Meeker, Denman & Co. Meeker sought additional means of revenue to buttress his trade and finance business.

As the war between France and Britain led to a critical demand for marine insurance, Meeker began to underwrite cargo brigs and schooners. He was on the Board of Directors of the Insurance Company of North America[1], and in 1802 was one of five men who established The Delaware Insurance Company of Philadelphia**.** At the same time, Meeker also began participating in a new economic sphere, banking.

The Philadelphia Bank

Capital and credit were tied up by wartime activities, as well as by the sole three banks run by a small clique of established gentry in Philadelphia. Fresh leadership was needed to break these barriers and crack the dominance of this aristocratic circle. A few lesser-known but determined young men gathered to exploit the possibilities and form a new bank. It was a natural progression for Meeker, who already had experience in large financial transactions; this relatively new economic paradigm offered him new sources of income by way of good investment return on stock.

The Philadelphia Bank opened its doors in 1803 in a rented home across the street from the Bank of North America on Chestnut Street. The concept of the new bank was novel. Credit was extended to groups previously excluded, such as mechanics and tradesmen; shares in the venture were priced lower; and the loans had longer terms. The 16 directors, including Samuel Meeker, deposited the bank's money in a box at the Bank of Pennsylvania, ordered "a proper set of books, stationery, scales, weights, shovels and other materials," and drafted rules and regulations. The first loan the bank made, on September 14, 1803, was to director Samuel Meeker, endorsed by his firm, Meeker, Denman & Co.

A Stuart Portrait and a Villa on the Schuylkill

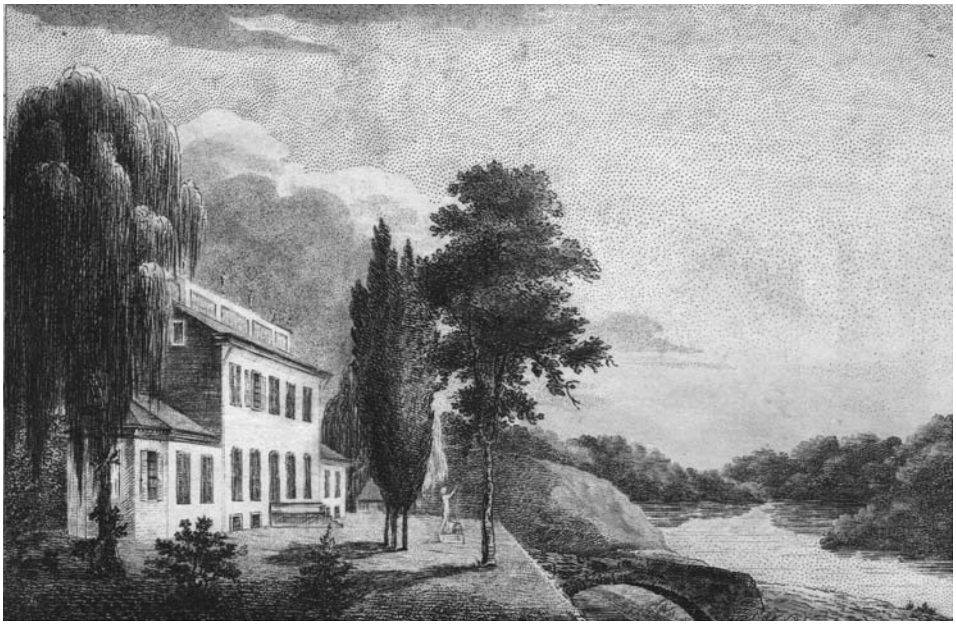
From 1796–1797 Philadelphia endured acute shortages of capital, as well as a severe yellow fever epidemic; financial panic caused massive economic disruption. Companies failed, and land values declined. Meeker positioned himself to take advantage of the reduced prices in real estate. In 1799, merchant Jonathan Mifflin, considered one of the wealthiest members of the family which produced Pennsylvania Governor Mifflin, lost several trading vessels *en route* to China and India. His country estate on the Schuylkill was taken over by the Bank of Pennsylvania and put on the market, where it remained unsold for almost two years before Meeker purchased it in the summer of 1802.

The banks of the Schuylkill, tributary to the Delaware River, was the new suburb of wealthy urban Philadelphians, providing summer retreats from Philadelphia's sewerless streets and overcrowded conditions. The country homes also protected against the feared and deadly epidemics of yellow fever, which periodically swept through the city. Meeker's villa, called Fountain Green, was not a palatial estate, but compact and of high quality. There he could associate with his peers, offer genteel hospitality to friends and family and make an elegant display of the prevailing symbols of wealth. Importantly, such manifestations inspired even more trust in the word and capability of the merchant.

By 1803 Philadelphia merchants had derived rich benefits from the war by taking advantage of American neutrality. Meeker's ambition served his ascent into wealth, enabling him to commission the Gilbert Stuart portrait that year and to display it appropriately to his peers in his villa on the Schuylkill River.

After completing a series of Washington portraits, Stuart commanded prices only exceeded by the best English portrait painters. During a 40th birthday celebration in honor of Samuel and Phoebe in 1803, Samuel presented the portrait of himself as a gift to his twin sister. The setting for the entertainment and display of the new portrait was Fountain Green.

Meeker had achieved prosperity as an esteemed merchant and the creator of new flows of capital. He also earned the respect of his peers by engaging in civic activities. As a young man in his mid-30s, he set aside his business concerns to aid the sick as an appointed health inspector during the yellow fever epidemic of 1797. He was a member of the Hibernian



William Birch illustration of Fountain Green, Samuel Meeker's villa on the banks of the Schuylkill River.

Society, providing new and poor emigrants with funds, jobs and medical care. He was athletic, with superb equestrian skills as described by other members in the Gloucester Fox-Hunting Club. His military career spanned from 1787 to 1812.

With war against England approaching, Meeker forecast that real estate values would fall once again. Before the War of 1812 could hammer his financial portfolio, Meeker sold Fountain Green to Thomas Cadwalader for $24,613.52 in silver in the Fall of 1809.[2] Although Meeker's original purchase price is not recorded, in light of the poor state of the economy and the number of distressed properties on the market at the time, it would likely have been substantially less. Cadwalader only possessed the villa for a brief period, as he apparently did not foresee the impact of war on the price of land. He was forced to sell Fountain Green in 1812 for $8,000 to a beer brewer, incurring a substantial loss on the transaction. Eventually another brewer purchased Fountain Green and used the high river bank for digging long tunnels to store lager beer. Later, the old home burned to the ground by a fire caused by a spark from a locomotive on the railroad built alongside the river.

Although the evidence portrays Samuel Meeker as achieving his path to prosperity and attaining entry into the highest levels of the mercantile and social elite of Philadelphia, this was not enough to prevent obscurity from settling over him with the passage of time. Ironically, what ultimately spurred historical interest in Meeker was not his familial connections, nor his social and financial skills, nor ownership of the celebrated Fountain Green villa on the Schuylkill River, but the Gilbert Stuart portrait given as a birthday present to his twin sister.

As art historian William Dunlap wrote of Stuart: "He left us the features of those who have achieved immortality for themselves, and made known others who would but for his art have slept in their merited obscurity."

Meeker eventually moved to Butler County, PA, and died in Portsmouth, Dauphin County, PA, on September 2, 1832. Perhaps his greatest dream did not come to fruition. His only son, Samuel Hampton Meeker, was not able to carry on the family business, as he died in 1822 at the age of 26. The Stuart portrait given to Phoebe has been passed down through the generations and remains in family hands. $

Elizabeth Ahrens-Kley is a descendant of Phoebe Meeker and owner of the Gilbert Stuart portrait of Samuel Meeker. For comments, e-mail the author at bethjena@gmail.com.

Notes

1. The Insurance Company of North America was the first American insurance company to issue life insurance, for a sea captain against death at sea or at the hands of Barbary pirates.
2. In contrast, Lansdowne was bought by Bingham for $31,050 in 1797. The earliest recorded price prior to Meeker purchasing the property was 140 English pounds in 1792.

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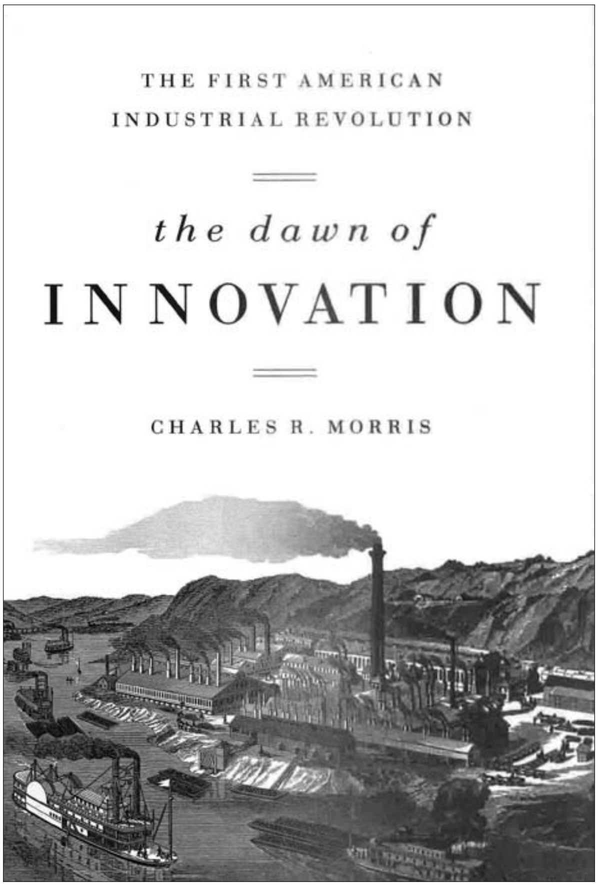
The Dawn of Innovation: The First American Industrial Revolution



By Charles R. Morris
Public Affairs, 2012
368 pages, $28.99

In an unusually descriptive Introduction, Charles R. Morris labels *The Dawn of Innovation* an intentional prelude to his 2005 book *The Tycoons*. That effort followed Andrew Carnegie, Jay Gould, J.P. Morgan and John D. Rockefeller as they helped make the United States the world's number one economic power after the Civil War. This book explores the earlier work of men who laid the foundations of that economic system that eventually overtook all others. Two concluding chapters serve as an epilogue and prologue as they summarize some post-Civil War accomplishments and ask whether China is positioned to overtake the US as the US once overtook Great Britain. These unnecessary but harmless detours do nothing to mar the author's compelling account of some familiar and unfamiliar aspects of America's economic past.

Instead of telling a chronological narrative, Morris conveys his story through a series of vignettes depicting various aspects of the evolving American economy. He ranges across space and time, describing the process of shipbuilding on the Great Lakes during the War of 1812 and the Colt Manufacturing presentation at the 1851 Great Crystal Palace Exhibition in London. In between, the book details familiar stories about textile mills and rifle manufacturing facilities in New England, and unfamiliar ones about pork processing in Cincinnati and western steamboats on midwestern rivers. In covering such a range of activities, Morris documents the distinctiveness of what came to be called the American system of manufacturing, as well as its ubiquitous nature.

Early on, Morris describes "hyperpower" Great Britain's 18th and early 19th century industrial revolution, recounting the accomplishments of more than a dozen innovators from Richard Arkwright to John Wilkinson. For several generations, that country's most creative minds took advantage of its geographic and natural resources, abundant supply of capital and high regard for commercial endeavors.

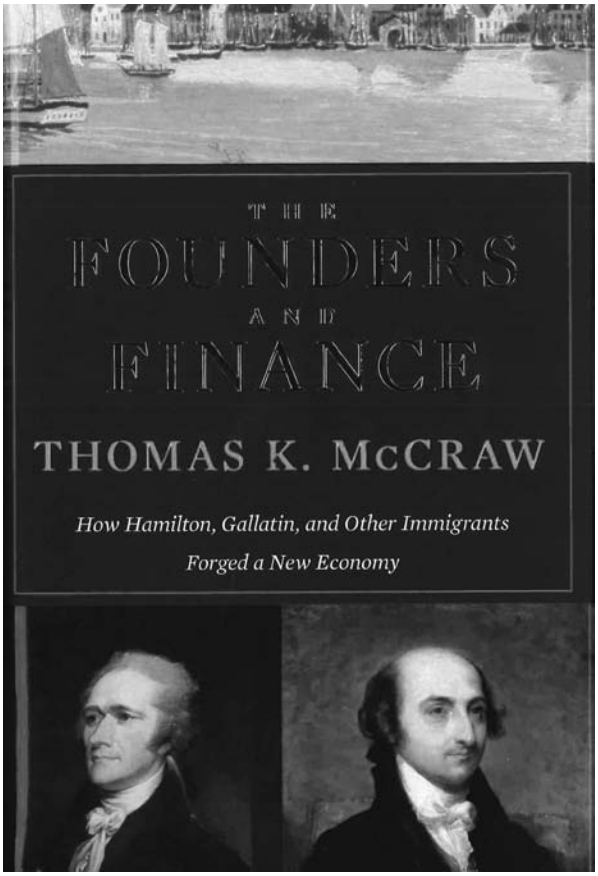
Morris suggests that the British eventually became complacent about their industrial prowess, particularly after using naval technology to defeat Napoleon. Throughout the book, he notes the growing economic competition between the established Great Britain and the emerging US. However, it is not at all clear that the advancements he traces in American manufacturing, transportation and agriculture should have been accompanied by concomitant declines in comparable British endeavors. What is clear is the assertion that American advances involving steamboats, arms manufacturing and clock-making sprung independently out of the minds of individual innovators and were not the result of a governmental edict or even a governmental policy that devoted resources to encouraging such innovations.

Morris differentiates his account of early 19th century American technological successes with two literary devices not present in other accounts of that period. One is a set of detailed illustrations that complement his words and help the reader appreciate many innovations in manufacturing clocks, guns and several types of machinery.

The other consists of contemporary observations of the American scene by best-selling authors such as Frances Trollope, Charles Dickens and Alexis de Tocqueville. Those voices confirm the author's contention that Americans had some very different attitudes than Europeans about work, innovation and social mobility. They also buttress his suggestion that the mass distribution of consumer goods to the broad middle class of society was as important to American manufacturers as the mass production of those products.

The Dawn of Innovation does indeed stand as a useful depiction of activities occurring before America's (Second) Industrial Revolution, when steel, electricity and railroads replaced iron, water power and steamboats as the engines of economic progress. $

The Founders and Finance: How Hamilton, Gallatin and Other Immigrants Forged a New Economy



By Thomas K. McCraw
Belknap Press, 2012
496 pages, $35

Alexander Hamilton and Albert Gallatin were both born outside North America. They were also both highly influential in establishing the initial financial infrastructure of the United States. In *The Founders and Finance*, Thomas McCraw explores the connection between those two statements. He uses most of the book to describe the lives and financial contributions of his two main protagonists. In several concluding chapters, the late Professor McCraw defends his conviction that their immigrant status gave Hamilton and Gallatin a special perspective on the financial needs of the fledgling nation and a concomitant ability to address those needs.

Few readers of *Financial History* need a primer on the accomplishments of Alexander Hamilton, and they will find no new information in this recounting of the facts. In keeping with his thesis, however, McCraw sprinkles his version of these familiar actions with comments about the influence his immigrant status may have had on this young man as he formed his views about the financial characteristics of the new nation.

Not being a Virginia landowner, New England merchant or Philadelphia lawyer, Hamilton may indeed have had a greater interest in the financial health of the entire nation than did contemporaries tied by blood to their states. Whether or not this is true, McCraw notes that while men such as Thomas Jefferson and James Madison were reviewing the political history of other republics as they sought to create a new type of relationship between a country's government and its people, Hamilton was reviewing the financial history of the European powers. In the same way that the nation's political founders created a form of government not seen anywhere else, this precocious financial thinker formulated a set of national economic policies that were just as revolutionary.

McCraw's section describing Albert Gallatin's distinguished career brings much-deserved attention to the accomplishments of this Swiss-born politician, diplomat, linguist, ethnologist and long-time Secretary of the Treasury. After some limited success in agriculture and real estate, in 1790 Gallatin found his true calling as a politician with a strong aptitude for financial matters. While serving in the Pennsylvania House, the US Senate and the US House, he was critical of Federalist policies on taxation, debt and military expenditures.

In 1802, President Thomas Jefferson asked Gallatin to be his Secretary of the Treasury and to "expose the blunders and frauds of Hamilton" as they combined forces to reverse many Federalist polices. Over time, however, Gallatin broke with Republicans on many financial issues. He saw little rationale for the Embargo Act and was in favor of both the Bank of the United States and federal spending on roads and canals. McCraw ascribes Gallatin's eventual agreement with much of Hamilton's financial decisions to his status as a "nationalist" with more interest in the country's economic prosperity than that demonstrated by sectionally-motivated politicians such as Jefferson and his successor and fellow Virginian James Madison.

In an interview shortly after publication, McCraw admitted it was impossible to prove his contention that Hamilton's and Gallatin's immigrant statuses gave them a special ability to devise the appropriate financial policies for the new nation. Yet, he noted that four of the first five Presidents were slave-holding Virginia planters, and he suggested that their worldview undoubtedly affected the decisions they made while in office. Isn't it reasonable to suggest that the worldview of two financially-astute men with little inborn allegiance to a particular state or region of the country affected their vision for their adopted country's economic health? Read *The Founders and Finance*, and decide for yourself. $

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Repudiation

continued from page 29

This was not a surprise. Basically, no important legislation, especially any dealing with the public debt, would become law as the 1868 elections had appeared on the horizon. Any reordering or refunding of the debt threatened the basis of the Democratic electioneering issue of greenback repayment. So, it was in the interest of Democratic Congressmen and the Democratic President to create as much gridlock as possible in the run up to the 1868 elections.

It was only after the Republican victories in 1868 that attention could again be focused on refunding the debt at a lower rate of interest. The Democratic gridlock was broken, and the Republicans seemed in a rush to permanently put the whole matter of the debt to rest. There was no more political advantage to be gained from a crisis surrounding the debt for the Republicans. In fact, with the popularity of the "Ohio Idea," the debt crisis had almost been successfully turned against them by the Democrats, causing panic in the Republican ranks. It was time for the Republicans to move on, and quickly.

Grant's Secretary of the Treasury was George S. Boutwell. His ideas on refunding were embodied in a law passed on July 14, 1870. The act authorized the Secretary, at his discretion, to issue $500 million in 10-year bonds at 5%, $300 million in 15-year bonds at 4.5% and $1 billion in 30-year bonds at 4%. These bonds were to be paid in gold. And, though it would take years for the total refunding to be accomplished, the 1870 act closed the book on the repayment crisis and the refunding crisis.

After 1870, the public debt receded from the public's attention. It continued to be reduced, as it had for years prior. It continued to be restructured, as it had since 1866. Taxes were collected and interest payments made as they had since the end of the Civil War. Repayment and management of the public debt remained on its established, dreary, steady course. Yet there was no longer a debt crisis. Where had it gone?

The debt crisis ceased to exist because there was no longer a political need for it. The Republicans had exploited anxiety over the public debt for its full worth, whipping up potential threats to the sacred debt into panics and crises for political gain. The party then hastily smothered the fire it created when it threatened to be successfully used against them by the Democrats.

The Democrats, in turn, had played up to lower class fear and resentment by creating the "Ohio Idea" of paying off the debt in devalued currency and using it to attack the Republicans. They also delayed Republican refunding efforts by causing Congressional gridlock in the run up to the 1868 elections.

Ultimately, it was not the unprecedented dollar amount of the public debt that created a debt crisis after the Civil War, but the public debt's unprecedented symbolic importance to the American people. **$**

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HOW MUCH DO YOU KNOW ABOUT FINANCIAL HISTORY?

TRIVIA QUIZ

By Bob Shabazian

1. What do super storm Sandy and the historic stock market crash of 1929 have in common?

2. What four financial institutions merged in 1949 to form the Midwest Stock Exchange?

3. Three of the five worst days in the history of the S&P 500 Index occurred on what day of the week?

4. What did the Currency Act of 1900 do?

5. President Franklin D. Roosevelt named Joseph P. Kennedy to head what government agency?

6. Karen N. Horn was the first woman to serve as president of a Federal Reserve Bank. In which district did she serve?

7. What was the first railroad to trade on the New York Stock and Exchange Board (later renamed the NYSE)?

8. When and where did organized options trading begin in the United States?

9. What publicly-traded utility company has paid a common stock dividend for more than 100 consecutive years?

10. Who was Benjamin Strong, Jr.?

1. Both occurred in the last week of October. **2.** The Chicago Stock Exchange, the Minneapolis-St. Paul Stock Exchange, the Cleveland Stock Exchange and the St. Louis Stock Exchange. **3.** Monday. **4.** It put the United States on the Gold Standard. **5.** The Securities and Exchange Commission. **6.** Cleveland. She served as president from 1982–1987. **7.** The Mohawk and Hudson. **8.** In 1973, with the opening of the Chicago Board Options Exchange (CBOE). **9.** Public Service Electric & Gas Company (PSE&G). **10.** First governor (title later changed to president) of the Federal Reserve Bank of New York.